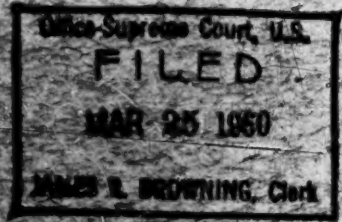


FILE COPY



No. 618—

**In the Supreme Court of the United States**

**October Term, 1959**

**UNITED STATES, PETITIONER**

**v.**

**CANNELTON SEWER PIPE COMPANY**

**ON WRIT OF HABEAS CORPUS TO THE UNITED STATES COURT OF  
APPEALS FOR THE SEVENTH CIRCUIT**

**APPENDIX B TO BRIEF OF THE UNITED STATES**

**Part I: Past and Present Legislative Materials and Treas-  
ury Department Reports, 1912-1954**

**Part II: Additional Legislative Materials: Excerpts From  
Hearings and Debates Indicating the Commercially Mar-  
ketable Products to Which the Proponents of Legislation  
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**Part I: Pertinent Statutes, Legislative Materials and Treasury Regulations, 1913-1954**

**1913**

**Income Tax Act of 1913**

**(c. 16, 38 Stat. 114, 166)**

**SECTION II**

**B. \* \* \***

That in computing net income for the purpose of the normal tax there shall be allowed as deductions: \* \* \* sixth, a reasonable allowance for the exhaustion, wear and tear of property arising out of its use or employment in the business, *not to exceed, in the case of mines, 5 per centum of the gross value at the mine of the output for the year for which the computation is made, \* \* \*. [Italics supplied.]*

**G. \* \* \***

(b) Such net income shall be ascertained by deducting from the gross amount of the income of such corporation, joint-stock company or association, or insurance company, received within the year from all sources, \* \* \* and in the case of mines a reasonable allowance for depletion of ores and all other natural deposits, not to exceed 5 per centum of the gross value at the mine of the output for the year for which the computation is made; \* \* \*.

**Treasury Regulations 33 (1914 ed.)**

**Art. 142.** *The term "gross value at the mine," as used in paragraphs B and G of section 2 of the act of*



October 3, 1913, prescribing a limit to the amount which may be deducted in the return of individuals and corporations as depreciation in the case of mines, *is held to mean the market value of ore, coal, crude oil, and gas at the mine or well, where such value is established by actual sales at the mine or well; and in case the market value of the product of the mine or well is established at some place other than at the mine or well, or on the basis of the bullion or metallic value of the ore, then the gross value at the mine is held to be the value of the ore, coal, oil or gas sold, or of the metal produced, less transportation, reduction, and smelting charges. [Italics supplied.]*

If the rate of 5 per cent per annum shall return to the corporation its capital investment prior to the exhaustion of the deposits, the rate on which the annual deduction for depletion of deposits is based must be lowered in accordance with the estimated number of years it will take to exhaust the estimated reserves.

In case the reserves shall be in excess of the estimates, no further deduction on account of depletion shall be made where the capital investment has been returned to the corporation.

1916

Revenue Act of 1916

(c. 463, 39 Stat. 756, 759)

SEC. 5. That in computing net income in the case of a citizen or resident of the United States—

(a) For the purpose of the tax there shall be allowed as deductions—

\* \* \* \* \*

Eighth. (a) In the case of oil and gas wells a reasonable allowance for actual reduction in flow and production to be ascertained not by the flush flow,

but by the settled production or regular flow; (b) in the case of mines a reasonable allowance for depletion thereof *not to exceed the market value in the mine of the product thereof, which has been mined and sold during the year* for which the return and computation are made, such reasonable allowance to be made in the case of both (a) and (b) under rules and regulations to be prescribed by the Secretary of the Treasury: *Provided, That* when the allowances authorized in (a) and (b) shall equal the capital originally invested, or in case of purchase made prior to March first, nineteen hundred and thirteen, the fair market value as of that date, no further allowance shall be made. \* \* \* [Italics supplied.]

1918

Revenue Act of 1918

(c. 18, 40 Stat. 1057, 1066)

SEC. 214. (a) That in computing net income there shall be allowed as deductions:

(10) In the case of mines, oil and gas wells, other natural deposits, and timber, a *reasonable allowance for depletion* and for depreciation of improvements, according to the peculiar conditions in each case, *based upon cost* including cost of development not otherwise deducted: *Provided, That* in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: *Provided further, That* in the case of mines, oil and gas wells, discovered by the taxpayer, on or after March 1, 1913, and not acquired as the result of purchase of a proven tract or lease, where the fair market value of the property is ma-

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terially disproportionate to the cost, the depletion allowance shall be based upon the fair market value of the property at the date of the *discovery, or within thirty days thereafter*; such reasonable allowance in all the above cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee; [Italics supplied.]

\* \* \* \* \*

1921

Revenue Act of 1921

(c. 136, 42 Stat. 227, 239)

SEC. 214. (a) That in computing net income there shall be allowed as deductions:

\* \* \* \* \*

(10) In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost including cost of development not otherwise deducted: *Provided*, That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: *Provided further*, That in the case of mines, oil and gas wells, discovered by the taxpayer, on or after March 1, 1913, and not acquired as the result of purchase of a proven tract or lease, where the fair market value of the property is materially disproportionate to the cost, the depletion allowance shall be based upon the fair market value of the property at the date of the discovery, or within thirty days thereafter: *And provided further*, That

such depletion allowance based on discovery value *shall not exceed the net income*, computed without allowance for depletion, *from the property* upon which the discovery is made, except where such net income so computed is less than the depletion allowance based on cost or fair market value as of March 1, 1913; such reasonable allowance in all the above cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee; [*Italics supplied.*]

\* \* \*

[Section 234(a)(9) (42 Stat. 256), applying to corporations, is the same as Section 214(a)(10), applying to individuals.]

H. Rep. No. 275

(67th Cong., 1st Sess., pp. 14-15 (1939-1 Cum. Bull.  
(Part 2) 181))

[14] \* \* \*

Section 214 allows substantially the same deductions in computing net income as are authorized under existing law, but adds the following provisions:

\* \* \*

[15] \* \* \* (6) *in order to make it certain that the depletion deduction when based upon discovery value shall not be permitted to offset or cancel profits derived by the taxpayer from a separate and distinct line of business*, it is provided that the depletion allowance based on discovery value shall not exceed the net income, computed without allowance for depletion, from the property upon which the discovery is made, except where such net income so computed is less than the depletion allowance based on cost or the fair market value as of March 1, 1913; \* \* \* [*Italics supplied.*]



## Treasury Regulations 62 (1922 ed.)

Art. 201. Depletion of mines, oil and gas wells; depreciation of improvements.— \* \* \*

(h) Depletion allowance in case of discovery: The deduction for depletion in case of a discovery can not exceed the net income computed without allowance for depletion, from the property upon which the discovery is made, except where and to the extent that such net income so computed is less than the depletion allowance based on cost or fair market value as of March 1, 1913. *Net income is the gross income from the sale of all mineral products and any other income incidental to the operation of the property for the production of the mineral products, less operating expenses, including depreciation on equipment, and taxes, but excluding any allowance for depletion.* If the mineral products are not sold as raw material but are manufactured or converted into a refined product, then the gross income shall be assumed to be equivalent to the market or field price of the raw material before conversion. Operating expenses, depreciation, and taxes on the property upon which the discovery is made, should be applied against the gross income from the same property on the basis of actual expenditures, but if the records for the year 1921 are in any case inadequate, allocation of such expenditures for that year may be made on the basis of the ratio of (1) the number of wells operated on the property on which the discovery is made to (2) the total number of wells operated in the operating division in which the discovery is included. [Italics supplied.]

1924

## Revenue Act of 1924

(c. 234, 43 Stat. 253, 258, 269)

## SEC. 204. \* \* \*

(c) *The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the same as is provided in subdivision (a) or (b) for the purpose of determining the gain or loss upon the sale or other disposition of such property, except that in the case of mines, oil and gas wells, discovered by the taxpayer after February 28, 1913, and not acquired as the result of purchase of a proven tract or lease, where the fair market value of the property is materially disproportionate to the cost, the basis for depletion shall be the fair market value of the property at the date of discovery or within thirty days thereafter; but such depletion allowance based on discovery value shall not exceed 50 per centum of the net income (computed without allowance for depletion) from the property upon which the discovery was made, except that in no case shall the depletion allowance be less than it would be if computed without reference to discovery value. [Italics supplied.]*

\* \* \* \* \*

SEC. 214. (a) In computing net income there shall be allowed as deductions:

\* \* \* \* \*

(9) In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. In

the case of leases the deduction allowed by this paragraph shall be equitably apportioned between the lessor and lessee;

[Section 234(a)(8) (43 Stat. 283), applying to corporations, is same as Section 214(a)(9), applying to individuals.]

### 1926

[Provision for *percentage depletion on oil and gas* was first made by Section 204 of the Revenue Act of 1926, c. 27, 44 Stat. 9. The provision was added by the Senate Finance Committee and allowed a 25 percent rate of depletion. This was amended on the Senate floor to allow a 30 percent rate. In conference the rate was reduced to 27½ percent. Prior to the enactment of this statute hearings were held before the House Ways and Means Committee, the Senate Finance Committee and the Senate Select Committee on Investigation of the Bureau of Internal Revenue and each of these committees issued reports on the subject. There follows in chronological sequence material portions of these hearings and reports, congressional debates on the subject and the text of the statute together with the Treasury Regulations adopted thereunder.]

### House Hearings, 1925

(Revenue Revision, 1925, Hearings Before the Committee on Ways and Means, House of Representatives)

[161]

### DISCOVERY AND DEPLETION

Statement of A. W. GREGG, Solicitor of Internal Revenue, TREASURY DEPARTMENT.

Mr. GREGG. Mr. Chairman and gentlemen of the committee, the next matter is the question of dis-

covery and depletion. Depletion is based upon the value of the property at the date of discovery in the case of oil wells, mines, etc. We discussed that in 1922. Since then the department has looked into several things which we think should be called to the attention of the committee. The discovery provision was first put into the statute to encourage the development of the natural resources of the country, primarily during the war, in 1918 for the first time. Under that provision, the discoverer, or the taxpayer who discovers an oil well, for example, can set up as the basis of depletion the value of the oil well at the date of discovery, and in making the deduction against the income from the operation of the oil well, the deduction is based upon the value at the date of discovery. I will give the history of that law: The deduction was unlimited under the 1918 act, and under the 1921 act it was limited to 100 per cent of the profits of the property upon which discovery was made. Under the act of 1924, you cut that to one-half and made it 50 per cent of the income from the property upon which discovery was made. That, it would seem, took care of the limitation of the deduction in the cases where the discovery value is properly given, but there are cases under the existing law where the taxpayer who is not really entitled to the discovery provision can get it.

\* \* \*

[163] THE CHAIRMAN. Mr. Gregg, I might as well say at this point that if I had my way I would wipe out this discovery depletion entirely. I consider that it might have been justified in time of war, and that was the only justification given for it to begin with—for the purpose of inducing men to go ahead and make these discoveries. At the time we put that in, as I recollect it, it was practically admitted that in

normal times they would not be entitled to anything of that kind.

**Partial Report of the Select Committee on Investigation of the Bureau of Internal Revenue, 1926**

(Investigation of the Bureau of Internal Revenue, S. Rep. No. 27, 69th Cong., 1st Sess. (commonly called the Couzens report, published in January 1926).)

## INVESTIGATION OF THE BUREAU OF INTERNAL REVENUE

January 7 (calendar day, January 12), 1926.—  
Ordered to be printed with illustrations.

Mr. Couzens, from the Select Committee on Investigation of the Bureau of Internal Revenue, submitted the following PARTIAL REPORT [pursuant to S. Res. 168, 68th Cong.].

Under Senate Resolution 168, Sixty-eighth Congress, First Session, adopted March 12, 1924, your special committee was appointed and directed to investigate the Bureau of Internal Revenue and report its findings together with recommendations for corrective legislation.

### [2] SUMMARY OF FINDINGS

The findings of this committee upon the subjects covered by this report, may be briefly summarized as follows:

#### [3] *Discovery depletion*

Discovery depletion is an exemption from taxation upon realized increment in value; not enjoyed by other taxpayers. Upon a tax rate of  $12\frac{1}{2}$  per cent; this exemption to the oil industry alone amounts to approximately \$37,500,000 annually, and during the



high-tax period it was correspondingly greater. But a minor part of this exemption is received by the wild-catter or prospector for whose benefit it was intended. The major portion of this exemption goes to the large oil-producing companies, which also deduct the prospecting and developing expense, intended to be offset by discovery depletion, from income as operating expense.

The regulations governing discovery depletion do not confine this exemption to the discovery of new deposits, but permit the blanketing of known pools of oil with discovery values, to be depleted, free of tax.

The statutory limitation of the value to be depleted, to that evident on the date of discovery or within 30 days thereafter, is ignored by the Commissioner of Internal Revenue, and indefinite periods of time are allowed, within which to fully develop values, to be deducted from taxable income as discovery depletion.

It is very clear that the purpose of the provision for discovery depletion was to stimulate prospecting for new deposits of mineral and oil, yet the allowance of discovery depletion is not confined to the taxpayers who discover new deposits of mineral or oil, nor to deposits discovered since March 1, 1913, but is allowed to taxpayers who develop discoveries made by others, and upon deposits known to exist prior to March 1, 1913.

### *Depletion of values determined by analytic appraisals*

Analytic appraisals, which determine values to be depleted by discounting estimated expected profits, are too elastic and leave too much to the judgment of individual engineers to be suitable for taxation purposes. An amendment of the law is required to permit the substitution of a more suitable method. A substitute method is described herein.

There has been a growing tendency, on the part of

authorities in the Bureau of Internal Revenue superior to the engineering valuation sections, to set aside sound determinations of values to be depleted, and to substitute excessive values, based upon analytic appraisals, in which the value of manufacturing and sales profits are attributed to ores in the ground. This practice is forbidden by the regulations, but the regulations are being so generally ignored, in this respect, that an amendment to the law is considered necessary to prevent further discrimination.

[8] DEPLETION AND VALUATION OF NATURAL RESOURCES  
FOR DEPLETION AND INVESTED CAPITAL PURPOSES

*Special examples of depletion*

The enormous deductions either allowed or claimed in certain cases are astounding and bring out more clearly than any argument the need of proper regulation of this matter. The figures speak for themselves and will be given in three groups as in the case of our general statistics, inasmuch as they are taken from the same three sources.

[19] *Discovery depletion for relief of wildcatters*  
(1865-66)

An examination of the hearings before the Ways and Means Committee of the House and before the Finance Committee of the Senate, when the 1918 act was under consideration by these committees, shows that the purpose of the provision for discovery depletion was to stimulate wildcatting or prospecting for the oil and minerals then needed to carry on the war.

[20] It was to meet this situation that the discovery provision was put into the 1918 act.

*The situation intended to be met by the discovery provision has so changed that every reason advanced for its enactment has disappeared.*

Thus, neither the war necessity for an increased production, nor the high war tax, which it was claimed retarded production, can now be offered as justification for the continuance of this discriminating tax exemption.

*Large operating companies, not small wildcatters, beneficiaries of discovery exemption*

[23] *Discovery depletion not dependent upon discovery of deposit*

The language used in framing the discovery clause has permitted an administrative construction, which is far beyond, and at wide variance from, its obvious purpose.

[33] *Summary on discovery of profit*

[34] *It is therefore recommended that if discovery depletion is not entirely eliminated the law be so amended as to confine it to the discovery of a deposit.*

[45] *Depletion of intangible property*

[55] *Witherbee-Sherman and Co. (3054)*

This case illustrates in a most striking manner the effect of the inclusion of manufacturing profits in the value of ores in the ground.

The property involved is an iron mine located in the State of New York. The taxpayer operates a small smelter in which a very small part of the ore mined is converted into pig iron. The greater part of the ore is sold as ore and concentrates.

The metals valuation section valued this property as of March 1, 1913, for depletion purposes at the present value of the prospective profits to be derived from mining and selling ore and concentrates. On this basis a value of 38.9 cents per ton of ore was determined.

The Committee on Appeals and Review reversed the metals valuation section and allowed a value of \$10,500,000 and a depletion unit of 62.97 cents per ton. This difference in depletion results in a difference in tax for 1917 and 1918 of \$301,169.10. The same reserves and discount factor were used in both valuations. The only difference in the valuation is the expected profit per ton. *The \$10,500,000 valuation is based upon the profits, which are estimated as procurable if the taxpayer builds a blast furnace near New York City and converts its ore and sells it as pig iron. Thus, this valuation attributes to the ores in the ground the prospective manufacturing profits estimated to be derivable from a blast furnace which does not exist and from a business in which the taxpayer is not even engaged. Exception has been taken to valuations of ore in the ground which included manufacturing and selling profits earned by taxpayers. In this case this element does not exist in the taxpayer's business but is imported into it for the sole purpose of inflating a value for depletion purposes*

*Upon the theory applied in this case a valuation of a billion dollars could be justified by assuming that the taxpayer might go a [56] few steps farther and*

*convert his theoretical pig iron into theoretical watch springs.* [Italics supplied.]

*Intangible values not proper subject of depletion*

[57] It is therefore recommended that the depletion provision of the income-tax law be so amended as to define the subject matter of depletion as the tangible physical deposit and to prohibit the use of any valuation based on prospective earnings in all cases where the profits capitalized are to a material extent due to the manufacturing or marketing ability of the taxpayer or to extrinsic causes other than the possession of the mineral itself.

*[114] Analytical appraisal method not suitable for tax purposes*

[115] That such appraisals, involving to the extent they do, the uncontrollable judgment of appraisal engineers, are a source of endless controversy between the Income Tax Unit and taxpayers, is not only a fact, but is not at all surprising.

[116] Any just method of determining depletion which does not involve the necessity of appraising the value of property by analytical appraisals will not only stop manifest gross discrimination but eliminate from the administration of the law one of the most fruitful sources of controversy, facilitate the determination of tax liability, and eliminate a great burden of expense to both the Government and the taxpayers.

*Proposed substitute for analytic appraisal*

A method of determining depletion and depreciation allowances in certain cases by discounting actual



profits annually as earned is proposed for the committee's consideration and will be fully described.

\* \* \* \* \*

Senate Hearings, 1926

(Revenue Act of 1926, Hearings before the Committee on Finance, United States Senate, 69th Cong., 1st Sess. on H.R. 1.)

[147]

REVENUE ACT OF 1926

Investigation of Bureau of Internal Revenue,  
Wednesday, January 13, 1926.

UNITED STATES SENATE,

COMMITTEE ON FINANCE,

*Washington, D.C.*

The committee met, pursuant to adjournment, at 10 o'clock a.m., in room 312, Senate Office Building, Senator Reed Smoot (chairman) presiding.

Present: Senators Smoot (chairman), McLean, Curtis, Reed of Pennsylvania, Ernst, Stanfield, Wadsworth, Shortridge, Simmons, Jones of New Mexico, Gerry, King, Harrison, Bayard, and George.

Present also: Senators Couzens, chairman of the Select Committee Investigating Bureau of Internal Revenue, and Mr. L. C. Manson, counsel to that special committee.

The CHAIRMAN. If the committee will come to order we will proceed. Mr. Manson, you desire now to take up the question of depletion, as I understand it.

Mr. MANSON. I do; yes, sir.

The CHAIRMAN. You may proceed.

Statement of L. C. MANSON, Esq., counsel for the Senate Select Committee Investigating Bureau of Internal Revenue

\* \* \* \* \*

[148] Senator CURTIS. What section is that?

Mr. MANSON. That is section 214. The House has made some amendment to that section in the bill that is now before this committee. It is my judgment that the House amendment makes no material difference in the law. It cuts out the allowance of discovery values on proven areas unless the taxpayer enters into an agreement with the adjoining owner whereby he shares the cost of bringing in the discovered well.

[153] Mr. MANSON. \* \* \*

Now, what I am leading up to in connection with this is this proposition: In the consideration of depletion of oil wells, [154] particularly, if the Congress should consider the allowance of a flat rate or a flat percentage of operating income—

Senator CURTIS. I will state here that I was going to offer an amendment providing for a percentage.

Mr. MANSON. What I want to bring out is that one argument that might be raised against a flat rate is that you would be allowing a depletion where it is not now allowed.

I desire to call your attention to the fact that if there is anybody that is not getting depletion now, it is because he has overlooked his opportunity, and I doubt it.

The CHAIRMAN. The simplest way, I suppose, to obviate that would be to have a flat tax on the operating income.

Senator CURTIS. On the gross income.

Mr. MANSON. The committee that I represent has not taken any position with respect to the uneconomic soundness of discovery depletion, and I do not care to enter into any further discussion of it, other than I have done for the purposes of calling attention to the way it operates.

Senator REED of Pennsylvania. That is only going half way. Can you not give us any recommendations about the way this thing should be handled?

Mr. MANSON. Well, I can when I get through. I would rather cover some other phases of it because I have more reasons for the recommendations that I would make than those I have given.

[158] Mr. MANSON. Without going into detail on the matter of valuation for depletion purposes, I want to say that *I believe that it is absolutely imperative that some method of determining depletion be figured out as a substitute for the present method of basing it upon valuations.* I do not think that any method could lead to more discrimination between taxpayers than the method which is now being pursued. We have not investigated a single oil valuation where two parties were interested in the same property where there was not a difference of at least 100 per cent in values placed upon the same property for depletion purposes for different interests. [Italics supplied.]

[177] Mr. MANSON. I think it was apparent from the testimony adduced before the committee that the valuation method which I concede to be the only practical method available for arriving at values for depletion purposes is entirely unsuited to the purposes of taxation.

The CHAIRMAN. Do you not think that is necessarily so?

Mr. MANSON. I do not believe it possible to arrive at a valuation of a mine or an oil well for purposes of taxation by any method that will insure justice between taxpayers. I do not think it can be done. I think, for instance, the valuation made by the

bureau of the copper properties varied as much as 300 per cent. I do not question the honesty nor the ability of the men who made those widely varying valuations. I do not believe it possible for any two engineers to value a mine or an oil well and arrive at a result that is even comparable without consulting and compromising on matters of judgment.

The elements of judgment involved in making valuations of this class are so great and there are so many of them that you could take small differences or judgment on each item and when multiplied together they will run into at least 300 or 400 per cent, run into differences which result in discriminations in the same industry which are so great that it makes it entirely unsuitable for purposes of taxation. *I believe that it is absolutely necessary that some other means be found for determining depletion than basing it upon value.* [Italics supplied.]

\* \* \* \*

Senator REED of Pennsylvania. Now, what you are saying seems to me to go direct to the heart of the question that we are confronted with. As legislators we are interested in looking to the future and in establishing a rule that will work greater justice, and we are not here to try the rights or wrongs of what has passed. I want to ask you whether as a result of all your studies of this question you think a greater measure of justice in the long run could be established if we were to fix depletion allowance at an arbitrary percentage for all taxpayers on the selling value of their product?

Mr. MANSON. There is no doubt about it.

[178] Senator REED of Pennsylvania. You think that would work greater justice?

Mr. MANSON. It would work greater justice.

The CHAIRMAN. The operating income of the mine.

Mr. MANSON. What I want to say is this: That it was not my purpose in presenting these discrepancies in valuations here to impeach the ability nor the honesty of the men who made them. I presented all of these discrepancies for the purpose of illustrating the futility of trying to arrive at a just measure of depletion through appraisal methods.

[179] Senator REED of Pennsylvania. Let us assume that that point is settled and we are driven then to some arbitrary percentage method and consider only the copper industry which you are talking about. If we adopt an arbitrary percentage of the sale price of the product to allow that depletion, will not that do great injustice, because you cannot apply the same percentage to the Lake Superior project or the vertical veins at Butte or the Porphyry mines in Utah, because there are totally different geological questions there, and a percentage that might be proper for the Utah copper company would be all wrong for the Calumet and the Hecla.

Mr. MANSON. I think if you will apply your percentage to annual earnings instead of the selling price of copper, you will overcome practically all of those inequalities.

Senator SIMMONS. Would you not overcome that, Senator Reed, by fixing an arbitrary rate beyond which the reduction could not take place.

Senator REED of Pennsylvania. That still leaves us with the matter of valuation. You still would have to have this appraisal which Mr. Manson has so clearly shown is unreliable, and I agree with him.

The CHAIRMAN. It seems to me the operating income of these mines is the best possible basis for arriving at the amount of facts and do the least injustice.



[180] Senator REED of Pennsylvania. Mr. Manson has just suggested that you could give the mine owner an option either to take a depletion allowance of 20 per cent of his net income or a depletion allowance based on the actual cost to him, without any valuation at all.

Senator SHORTRIDGE. Senator Reed, your thought is applied to mine operations?

Senator REED of Pennsylvania. By "mines" I include all natural resources.

\* \* \* \* \*

[197] Statement of A. W. GREGG—Continued.

Mr. GREGG. On the matters that have been taken up to-day by Mr. Manson it seems to me that there are three points to discuss. \* \* \*

On the matter of future legislation I recognize, as Mr. Manson does, the difficulty involved in these analytical appraisals. I think everyone realizes and appreciates that. It comes down in the last analysis to a matter of judgment. The law requires that the judgment be exercised by someone. In the past I think it has been exercised certainly honestly and intelligently in the decisions of the cases. If something can be done, however, to relieve the department of the necessity of making those valuations it will certainly be a great step in advance.

Senator WATSON. Well, what could be done?

Mr. GREGG. That is what I was coming to. *It has been suggested that depletion could be computed on a basis of a percentage of the net income from the operation of the property, computed without any allowance for depletion. That would relieve the department of a great many difficulties if it were possible. [Italics supplied.]*

The objections that occur to me to such a system are these: In the first place, in your solid minerals, you

would very clearly have a different rate for each mineral. The soundness of the proposal would depend on the rate used. I do not think that we have now sufficient data to arrive at a proper rate. I tried at Senator Jones's request to get the data, and I got some with reference to oil and gas, which is not satisfactory, but I was not able in the time I had to get any with reference to solid minerals, particularly of the different types of solid minerals on which depletion is allowed.

Even if you have sufficient data to arrive at a proper rate, looking at the industry as a whole, it should be realized that that rate even in a single industry which is proper to apply to one deposit in one part of the country will be absolutely improper as applied to another deposit even of the same material in another part of the country where the expense of mining, the expense of production, the grade of the ore, may vary materially. The whole question comes down, if you have sufficient data to get a proper rate, as to [198] how far Congress would be willing to go in the interest of simplicity as against the exact logic of the question.

[199] Senator JONES of New Mexico. Now Mr. Gregg has said that he has been unable to arrive at a proper basis. What he means by a proper basis I do not quite understand. Or what particular facts he is seeking in order to get a proper basis I do not know. But clearly we are now supposed to give depletion based upon valuation of the property and various other things. Now it is true that any definite basis for deduction may be subject to criticism, but I think that we can reach a basis which is less subject to criticism than what we have in the law now.

Senator REED of Pennsylvania. Just because of that thought, and I confess that I have it as you have

expressed it, I would like to ask Mr. Gregg the same question that I asked Mr. Manson this morning. Suppose, Mr. Gregg, that you were the whole Congress of the United States, how would you handle this troublesome question of depletion?

Mr. GREGG. I do not know, Senator Reed. We have been thinking of it to my knowledge since 1922, trying to work out some plan. We thought then of the possibility of allowing arbitrarily a given percentage of the net profits from the operation of the mine or well as depletion. At that time we were all impressed with the inequities [200] of the situation, that that would result in grouping an entire industry at least under one head, giving each individual taxpayer within that group a rate of depletion based upon the average of the group, although it might bear no relation whatever to his own peculiar position. That objection still exists, of course. But if your rate gets low enough, in the interest of simplicity you can afford to be arbitrary and adopt a fixed rate admitting its arbitrariness and the inequalities which will result in individual cases from it.

\* \* \* \* \*

[202] Senator REED of Pennsylvania. Now, Mr. Gregg, I brought that up merely to illustrate what seems to me an insuperable difficulty in the calculation of percentages. Having said what I repeated, this Midcontinent representative then went on to say that the lowest possible percentage which could be arbitrarily set for their depletion would be 25 per cent of their gross income from oil and that anything less than that would not begin to compensate them for the disappearing capital in an oil well.

The CHAIRMAN. Well, that would be too much for a mine. You would not want that in copper.

Senator REED of Pennsylvania. Suppose you fixed that with their curves and charts in view, and they seem to make a good argument, if you apply the same rule to bituminous-coal mining not a single company in the United States will show any profit.

The CHAIRMAN. That is why I say there is the difference between the oil and the mineral.

Senator REED of Pennsylvania. *So if we are going to ask an arbitrary percentage it has got to be a different percentage for different industries.* [Italics supplied.]

Senator JONES of New Mexico. *And should it not be based on net income rather than gross income?* [Italics supplied.]

Senator REED of Pennsylvania. No. [Italics supplied.]

[203] Senator JONES of New Mexico. I was going to suggest this, that in lieu of discovery depletion, and so on, that we allow a certain percentage of their net income to be deducted from it.

Mr. GREGG. That is what I understand Senator Reed was discussing.

Senator REED of Pennsylvania. That is tantamount to the same thing.

The CHAIRMAN. Well, the net income, there is something in that.

Senator REED of Pennsylvania. It comes down to the same thing in the end exactly, whether you allow an arbitrary percentage of deduction of net income, or whether you arbitrarily reduce the tax rate which is based on the net income. \* \* \*

Senator SIMMONS. What is your proposition, Senator?

The CHAIRMAN. Well, there are two propositions. That you impose a tax of whatever percentage we

agree on the operating income derived from a mine, whether it be a well or whether it be copper or whatever it is. You take the operating income derived or the net income to that mine, and you then do not have to have anything to do with depletion. It is the production that counts. That is all there is to it. Now, the only trouble with that is between the oil and the metal mine. \* \* \*

[204]

Senator REED of Pennsylvania. I want to find out what the bureau has worked out in its studies. They have been trying to substitute something for it too. They are thinking along the lines that you and I are, Senator Jones, and I want to find out what position they have come to.

Mr. GREGG. That is what I said; we started on the percentage plan, and for the reasons which I stated to you, finally gave it up. Those reasons may not be insurmountable.

The CHAIRMAN. The percentage plan on what basis?

Mr. GREGG. Taxing the concerns on their net income without any deduction for depletion except an arbitrary percentage, 10, 20, 25 per cent of that net income computed without depletion.

S. Rep. No. 52

(69th Cong., 1st Sess., pp. 17-18 (1939-1 Cum. Bull. (Part. 2) 332, 345-346)

[17]

The administration of the discovery provision of existing law in the case of oil and gas wells has been very difficult because of the [18] discovery valuation that had to be made in the case of each discovered well.



*In the interest of simplicity and certainty in administration your committee recommends that in the case of oil and gas wells the allowance for depletion shall be 25 per cent of the gross income from the property during the taxable year. The provision of existing law limiting this amount to an amount not in excess of 50 per cent of the net income of the taxpayer from the property is retained. [Italics supplied.]*

Senate Debate, 1926

(67 Cong. Record (Part 4), 69th Cong., 1st Sess.  
(1926))

[3762] \* \* \*

MR. REED of Pennsylvania. I see the Senator's point. Will not the Senator let me explain what Congress has done and what the committee recommends now, and then we can go back to the more fundamental question which the Senator raises, as to whether either policy is right—that is, the past policy or the new one that we have recommended?

I hope I have explained to the Senate how this present method of calculating depletion in oil wells is really a combination of uncertainties. The factor of error that is possible in either of those elements is intensified by the fact that we are multiplying one uncertainty by another.

That leads to almost constant conflict between the oil-well operators and the bureau. There is hardly any important operator who does not have a lawsuit on every year's return, because he estimates that his depletion is, say, \$1.25 a barrel, and the bureau sends its engineers down, and they make guesses different from those of the taxpayer, and they say to him, "No; your depletion is only 30 cents a barrel." While that does not sound very large when applied to an important producing area, it means a difference of millions of dollars to the Government and to the taxpayers.

*So we are trying, by the Finance Committee amendment, to get away from those uncertainties and to adopt a rule of thumb which will do approximate justice to both the Government and the taxpayers.* [Italics supplied.]

*We find, then, that probably the best way to do it is to provide that an arbitrary percentage on the gross value of each year's yield be chalked off for depletion. We figure it on gross income instead of net income, because the net income from oil wells varies very greatly. When the first flush production comes the operating cost of the well is very low per barrel, but as the well trails down and finally comes to produce a small quantity of oil, the cost increases. Up in my State we have many wells working which average less than a quarter of a barrel of oil per day. Obviously, the operating cost of those wells is pretty high, and in many cases production gets down to the point where there is practically no net income, and yet the oil keeps flowing. There is a reduction of capital going on, and if we based the depletion on net income we would not always reflect it.* [Italics supplied.]

\* \* \* \* \*

[3763] Mr. REED of Pennsylvania. The Treasury Department selected at random 50 taxpayers engaged in the production of petroleum for the three-year period 1918, 1919, and 1920, and again for the three-year period 1921, 1922, and 1923. The result shows the percentage of depletion to gross income for those years, and I ask Senators to follow the figures carefully because some of them are pretty startling.

\* \* \* \* \*

[3764] Mr. COUZENS. How many companies were involved in those figures?

Mr. REED of Pennsylvania. Fifty companies. I may say that these 50 companies are none of them

engaged in marketing refined products. If we took cases involving such companies, we would get into complications of their income from refining operations and that would obscure the lesson we can draw from the figures.

[3767]

Mr. HARRELD. \* \* \*

I think the proposal to change the method of calculating the discovery depletion charge is very commendable, is very proper, and is right. \* \* \* All that a man is required to do is to report to the department his gross receipts from oil and take from it a depletion of 25 per cent. The only objection I can see to that is that I think it is not giving the producer of oil a sufficiently large percentage. In my judgment, it ought to be 35 per cent, and I may later offer an amendment to that effect.

[3772]

Mr. COUZENS. \* \* \*

Mr. President, much has been said about what this 25 per cent which is provided in the Finance Committee's amendment to this provision means.

After this amendment was first suggested in the Finance Committee by the senior Senator from Kansas [Mr. Curtis], the members of the investigating committee were asked, through Mr. Manson and myself, to ascertain what this would really mean, as far as they could. The conclusions reached, which are sub-

stantiated somewhat by these figures which I am now reading, were that a 25 per cent allowance on gross incomes meant in practice an allowance of 50 per cent on net incomes in all cases.

In other words, in some cases it might exceed the 50 per cent, but according to the statute the 50 per cent was the limit, and in no case could we find where it would be less than 50 per cent, so that in effect we might as well say that the discovery value allowed meant a reduction of 50 per cent of the net income in all cases. For example, we took 100 companies who reported in 1918. \* \* \*

H. Conference Rep. No. 356

(69th Cong., 1st Sess., pp. 31-32 (1939-1 Cum. Bull. (Part 2) 361))

[31]

\* \* \* \* \*

The administration of the discovery provision of existing law in the case of oil and gas wells has been very difficult because of the discovery valuation that had to be made in the case of each discovered well. *In the interest of simplicity and certainty in administration* the Senate amendment provides that in the case of oil and gas wells the allowance for depletion shall be 30 per cent of the *gross income from the property* during the taxable year. The provision of existing law limiting this amount to an amount not in excess of 50 per cent of the net income of the taxpayer from the property is retained.

The House recedes with an amendment providing that the depletion deduction based upon gross income in the case of an oil and gas well shall be 27½ percent of that income instead of 30 percent, and in the case of mines the Senate amendment is changed to provide that discoveries shall include minerals in commercial quantities contained within a vein or deposit discovered in an existing mine or mining tract by the

taxpayer after February 28, 1913, if the vein or deposit thus discovered was not merely the [32] uninterrupted extension of a continuing commercial vein or deposit already known to exist and if the discovered minerals are of sufficient value and quantity that they could be separately mined and marketed at a profit. [Italics supplied.]

Revenue Act of 1926

(c. 27, 44 Stat. 9, 14)

SEC. 204. \* \* \*

(c) The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the same as is provided in subdivision (a) or (b) for the purpose of determining the gain or loss upon the sale or other disposition of such property, except that —

(1) In the case of mines discovered by the taxpayer after February 28, 1913, the basis for depletion shall be the fair market value of the property at the date of discovery or within thirty days thereafter, if such mines were not acquired as the result of purchase of a proven tract or lease, and if the fair market value of the property is materially disproportionate to the cost. The depletion allowance based on discovery value provided in this paragraph shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property upon which the discovery was made, except that in no case shall the depletion allowance be less than it would be if computed without reference to discovery value. Discoveries shall include minerals in commercial quantities contained within a vein or deposit discovered in an existing mine or mining tract by the taxpayer after February



28, 1913, if the vein or deposit thus discovered was not merely the uninterrupted extension of a continuing commercial vein or deposit already known to exist, and if the discovered minerals are of sufficient value and quantity that they could be separately mined and marketed at a profit.

(2) *In the case of oil and gas wells the allowance for depletion shall be 27½ per centum of the gross income from the property during the taxable year. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph. [Italics supplied.]*

Treasury Regulations 69

(1926 ed.)

ART. 221. Depletion in the case of oil and gas wells—Under section 204(c)(2), in the case of oil and gas wells, a taxpayer may deduct for depletion an amount equal to 27½ per cent of the gross income from the property during the taxable year, but such deduction shall not exceed 50 per cent of the net income of the taxpayer (computed without allowance for depletion) from the property. In no case shall the deduction computed under this paragraph be less than it would be if computed upon the basis of the cost of the property or its value at the basic date, as the case may be. In general, "the property," as the term is used in section 204(c)(2) and this article, refers to the separate tracts or leases of the taxpayer.

1927

## Joint Committee Report on Depletion

(Preliminary Report—Depletion—Oil and Gas, Revenue Act of 1926, Report of the Joint Committee on Internal Revenue Taxation, Vol. 1—Part 2 (1927))

## [11] TENTATIVE NATURE OF THE REPORT

There is still another reason for making this report preliminary rather than final, which is that, in the case of the very large oil companies, the returns themselves must be analyzed. The gross income of these large oil companies arises from transporting, refining, and marketing oil as well as from producing. For the purposes of our study, *the gross income from production alone must be determined*. The statistics of the bureau do not segregate this income, and recourse must be had to the returns. The bureau has been requested to furnish the returns for 38 large oil companies. It will take some [12] little time before these returns may be secured without inconvenience to the bureau. [Italics supplied.]

## A. General Effect of 1926 Act

## OIL AND GAS DEPLETION

## 1. 1926 and 1924 Acts Compared.

The following definitions of certain words or phrases included in the above must be given in order to discuss the subject intelligently:

“From the property” is interpreted to mean from each individual tract or lease. In other words, the net or gross income must be computed not for all the prop-

erties of the taxpayer lumped together, but from each individual leasehold.

[13] "Gross income from the property" may be defined, therefore, for oil and gas properties, as *the gross receipts from the sale of oil and gas as it is delivered from the property less the royalties paid in cash, if any.* As it is not customary for operators to report oil royalties as a part of their receipts ordinarily, gross income will coincide with gross receipts. In the case of lessor interest, the royalty will represent the gross income from the property. *In the case of taxpayers who are operators, refiners, transporters, etc., the gross income from the property must be computed from the production and posted price of oil, as the gross receipts from a refined and transported product can not be used in determining the income as relating to an individual tract or lease.* [Italics supplied.]

"Net income from the property (computed without allowance for depletion)" may be defined as the gross income from the property as interpreted above, less the operating expenses, wages, repairs, taxes (except income taxes), losses not compensated by insurance, depreciation, and other legal deductions which can be specifically allocated to the individual tract or lease, and also less a reasonable amount of overhead, general and traveling expenses, etc., as may be properly prorated to this individual tract or lease.

## 2. Results of Change Made in 1926 Act.

The above comparison of the 1926 and 1924 revenue acts makes the following results self-evident as to the general effect of the 1926 act:

(a) It eliminates discovery depletion and the necessity for valuations as of date of discovery.

NOTE.—This result is beneficial to the bureau in that it reduces the valuation work. It is beneficial to the taxpayer in that he is relieved from supplying voluminous data on oil properties.

[14] (b) It retains the necessity for March 1, 1913, valuations.

NOTE.—This is not a serious matter as the great majority of such valuations have now been made.

(c) It retains the maximum limit for depletion at 50 per cent of the net income from the property.

(d) It retains the minimum limit for depletion on the basis of the cost or March 1, 1913, value of the property.

NOTE.—The same data must be kept for each property in regard to net income costs, and March 1, 1913, value under both the 1924 and 1925 acts; therefore there is no change in the administration of the features (c) and (d) described above.

(e) It allows an arbitrary  $27\frac{1}{2}$  per cent of the gross income from the property as depletion, if within the limits described in (c) and (d) above.

NOTE.—*As the gross income from each property is necessary in determining net income, there is no extra work of computing this provision. [Italics supplied.]*

On the whole, we may conclude, as far as the administration of the law is concerned, that the 1926 act requires less work and is simpler. As to the equity and effect on taxes of the provision, that will be discussed later.

1928

(Prior to the passage of the Revenue Act of 1928, c. 852, 45 Stat. 791, which rearranged the structure of



the revenue provisions, percentage depletion for metal mines was requested and an amendment allowing it was proposed on the House floor but was withdrawn for further study. More detailed Treasury Regulations relating to percentage depletion on oil and gas were also promulgated under the 1928 Act. The pertinent material is set forth below in chronological order.)

**House Hearings, 1927-1928**

(Revenue Revision, 1927-1928, Hearings before the Committee on Ways and Means, House of Representatives, Interim, 69th-70th Cong.)

[156] Brief submitted by Mr. PINKERTON on behalf of the Illinois Chamber of Commerce.

[161] DEPLETION (Section 202(b)(2), (c)(1))

The same objection as is made in reference to the adjustment of depreciation is made to the principles underlying the adjustment for depletion for previous years at the time of a sale.

Moreover, the ascertaining of depletion rates has caused enormous work both to the Government and the taxpayers in ascertaining the 1913 values of mines. The present value method is most elaborate and complicated. Of course, the ascertainment of the 1913 values is now disposed of, but similar questions come up every time the value of a discovery is to be ascertained. *It is submitted that a rule should be devised for depletion of mines similar to that provided in the 1926 act for oil and gas wells.* The 1926 act provides that in the case of oil and gas wells the depletion deduction shall be  $27\frac{1}{2}$  per cent of the gross incomes from the property during the taxable year but not more than 50 per cent of the net income of the taxpayer from the property, and also provides that in no case shall the depletion allowance be less than it



would be if computed without the benefit of this 27½ per cent provision. This does away with all the complicated procedure of ascertaining discovery values and also of dealing with depletion allowed or allowable, as the taxpayer under this method would continue to get depletion as long as he was mining and selling ore. [Italics supplied.]

[505] Statement of J. F. CALLBREATH, Washington, D.C., Representing the American Mining Congress.

[Sec. 204 (c)]

Mr. CALLBREATH. My name is J. F. Callbreath, and I am secretary of the American Mining Congress.

The CHAIRMAN. Let me ask if you are willing to be limited to five minutes?

Mr. CALLBREATH. Yes; I am.

We appear at this time, gentlemen of the committee, in the hope that we may lend some assistance to you in the simplification of the depletion clause of the revenue act as applied to metal mines.

On August 4 the Commissioner of Internal Revenue sent out this invitation:

The Joint Congressional Committee on Internal Revenue Taxation has begun a study of the depletion question in order to determine whether or not a percentage of income basis *similar to that now in effect in the oil and gas industry can be applied to the other natural resource industries.* [Italics supplied.]

As a preliminary I want to make that statement.

In accordance with that invitation the metal mining industry was not able to get together in such a way as to authorize our office to appear before you as representing the industry until Tuesday of this week. At that meeting, a resolution was adopted asking the presentation of a plan which contemplates changes in subdivision (c) of section 204. Those changes appear

in caps upon the slips with which you have been furnished.

[506] The metal-mining industry in compliance with the request of the Commissioner of Internal Revenue has submitted data with respect to the operations of the various metal mines throughout the United States for the purpose of assisting the Treasury Department in supplying information requested by the joint committee on internal revenue taxation in connection with its study of the depletion question *in order to determine whether or not a percentage-of-income basis similar to that now in effect in the oil and gas industry can be applied to other natural resource industries.* [Italics supplied.]

It is believed that the division of investigation of the joint committee has completed its study of the subject as far as the metal-mining industry is concerned and is now ready to supply the information necessary to determine just how the proposed plan, if adopted, would affect public revenue and in general of the merit the proposed plan might possess from the standpoint of the Government as well as the taxpayer.

Certain positive advantages of the proposed plan may be briefly summarized as follows:

It provides a simple, definite method, easy of application, that permits the prompt and final determination of the tax liability.

It makes for simplification and substantial economy in administration not only in that it removes the difficulties attendant to discovery valuations but furnishes a method for computing the depletion deduction readily susceptible of audit in the field, a distinct aid to the decentralization policy now in force in the Internal Revenue Bureau.

It obviates the uncertainty inherent in any valuation plan due to the necessity for the use therein of numerous more or less arbitrary factors.

It removes the discrimination against the large number of smaller taxpayers who do not have the technical staffs or who feel unwarranted in going to the expense of engaging the professional services necessary to the establishment of discovery depletion under the present plan.

It removes the uncertainties resultant from the present methods when the unit depletion deduction requires adjustment due to unavoidable errors in the original estimate of ore reserves.

[507] Numerous conferences have been held by representatives of the metal-mining industry during the last few months while the commissioner has been gathering the information requested, in order that the industry might have a full understanding of what might be proposed on a percentage basis. This series of conferences culminated in a meeting held November 1, 1927, at which more than 75 per cent of the metal-mine production of the United States was represented, and at which time the plan herewith submitted was unanimously approved. *This plan has the united support of all branches of the metal-mining industry and its early adoption is urged particularly in the interests of numerous small operators in the several metal-mining States who have been unable to take advantage of depletion allowances under the present law, on account of the great expense involved in the determination of valuation; and in particular the determination of discovery valuations under the present rulings and practices of the Bureau of Internal Revenue. [Italics supplied.]*

It is not the desire at this time to take up the time of your committee by an extended oral presentation of this matter, but *it is requested that the American Mining Congress, on behalf of the metal-mining industry of the United States*, be granted 10 days within which time to prepare and file a brief in support of an amendment making the proposed plan effective by Congress at its coming session. [Italics supplied.]

The CHAIRMAN. Very well; you may file a brief and supply the members with copies.

Mr. OLDFIELD. *Mr. Callbreath, are you trying to place the metal mining industry in the same position as the oil industry?* [Italics supplied.]

Mr. CALLBREATH. *As nearly as may be; yes, sir.* [Italics supplied.]

[508] Brief submitted by Mr. CALLBREATH for the American Mining Congress in behalf of the metal-mining industry of the United States.

#### PROPOSING AN AMENDMENT TO SECTION 204(c) OF THE REVENUE ACT OF 1926

Developments leading up to the submission of amendment proposed to section 204, subdivision (c).

*To the Honorable Members of the Committee on Ways and Means of the House of Representatives:*

The metal-mining industry, in compliance with the request of the Commissioner of Internal Revenue, has submitted data with respect to operations of the various metal mines in the United States, and those owned by American taxpayers in foreign countries. The purpose was to assist the Treasury Department in the compilation of information desired by the Joint Committee on Internal Revenue Taxation for use in



its study of the income tax law as relates to mine-depletion allowances. It has been understood that the purpose of the study on the part of the committee was to determine whether it is practicable to apply to the mining industry a percentage-of-income basis similar to that now in effect in the oil and gas industry.

It is believed that the division of investigation of the joint committee has completed its study of the subject as far as the metal-mining industry is concerned, and is now prepared to report on the merits of the proposed plan and to supply the information necessary to determine how it would, if adopted, affect the public revenue.

As a result of a concurrent study of the depletion question made by the metal-mining industry, the conclusion has been reached that the application of a percentage-of-income basis for the determination of the allowance for depletion in the case of metal mines is not only practicable but possesses certain important advantages from the standpoint of both the Government and the taxpayer.

It will be observed that the amendment proposed is a simple one which does not directly affect other provisions of the revenue act. Its adoption, therefore, will not make necessary any change in other portions of the act, nor will it in any way complicate other revisions which may be contemplated by Congress.

Briefly stated, the outstanding advantages of the amendment, which are discussed hereinafter, are, that without materially affecting the public revenue, it provides a simple, equitable, and definite method of computing the depletion allowance that permits of the prompt and final determination of the tax liability. It eliminates for the future the analytical appraisal of metal mines with attendant technical complexities. It means a great saving of expense to the Government



as well as the taxpayer. It removes all pretext for the objectionable recurring revaluations with which the industry has been confronted for years. It removes discrimination and gives to the smaller operator who can not now afford to spend the money necessary to establish proper value of his ore bodies and the corresponding depletion value of his unit of production, the reasonable allowance for depletion contemplated by the statute.

Provision for depletion as a deduction from income has been made in all of our income-tax laws and discovery depletion has been allowed specifically since 1918 and indirectly in the act of 1913. The deduction for depletion under the revenue act of 1916 was based upon either cost or the fair market value as of March 1, 1913. The revenue act of 1918 provided another basis, that of discovery value. With certain modifications there three bases have been carried down through the successive acts to date, the revenue act of 1926 at section 204(c) providing that the basis for the determination of the reasonable allowance for depletion authorized in section 234(a)(8) shall be cost, March 1, 1913, value, discovery value, and in the case of oil and gas wells, a fixed percentage of gross income.

The provisions of existing and earlier revenue acts employing a basic date method of valuation for the computation of depletion are and always have been based on sound economic principles, and for [509] lack of any experience as to means and results, it would have been unwise, if not impracticable, to have employed any other method. None the less, it always has been desirable to reach the same result by a shorter and simpler method. And now as a result of a practical experience of more than a decade in computing depletion on a valuation basis, it has become

possible to propose a definite rate of depletion for metal mines to govern in the future that will give assuredly a result fairly comparable to that obtained by valuation and without disturbing those valuations already agreed upon with the Treasury Department. Because of this experience, the rate proposed has a background of statistical authority.

The following proposed amendment is the result of numerous conferences attended by those interested in the metal-mining industry, and was unanimously approved by representatives of in excess of 75 per cent of the metal-mine production of the United States at a meeting held on November 1, 1927. It overcomes the numerous disadvantages of existing statute so far as metal mines are concerned.

*Proposed amendment of section 204(c) (changes shown in italics):*

“(c) The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be the same as is provided in subdivision (a) or (b) for the purpose of determining the gain or loss upon the sale or other disposition of such property, except that—

“(1) In the case of mines discovered by the taxpayer after February 28, 1913, the basis for depletion shall be the fair market value of the property at the date of discovery or within 30 days thereafter, if such mines were not acquired as the result of purchase of a proven tract or lease, and if the fair market value of the property is materially disproportionate to the cost. The depletion allowance based on discovery value provided in this paragraph shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property upon which the discovery was made, except that in no case shall the depletion allowance be less than it would be

if computed without reference to discovery value. Discoveries shall include minerals in commercial quantities contained within a vein or deposit discovered in an existing mine or mining tract by the taxpayer after February 28, 1913, if the vein or deposit thus discovered was not merely the uninterrupted extension of a continuing commercial vein or deposit already known to exist, and if the discovered minerals are of sufficient value and quantity that they could be separately mined and marketed at a profit. *This paragraph shall not apply to metal mines discovered after the effective date of this act.*

*"(2) In the case of metal mines the allowance for depletion shall be 15 per centum of the gross income from the property during the taxable year, such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowances for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.*

*"(3) In the case of oil and gas wells the allowance for depletion shall be 27½ per centum of the gross income from the property during the taxable year. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph."*

The figure of 15 per cent, here proposed, represents, to the best of the information available to the industry, an actual average of the depletion deductions which have been allowed by the Treasury Department under existing law during the past five years (1922 to 1926, inclusive), in each of the several branches of the metal-mining industry. From the information compiled by

the industry in response to questionnaires, it is believed that this figure will be substantiated by the studies of the division of investigation of the joint committee, which it is understood is prepared to report on the subject. The percentage depletion allowance here proposed is thus merely the equivalent of the actual allowances under previous revenue acts.

#### ADVANTAGES OF PROPOSED AMENDMENT

The percentage-of-income basis contained in the proposed amendment has the following distinct advantages: (1) Definite assurance of prompt and final settlement of tax liability; (2) simplification: [510] (3) economy of administration; (4) the removal of present uncertainties; (5) the avoidance of discrimination.

##### (1) Definite Assurance of Prompt and Final Settlement of the Tax Liability.

The percentage method of determining the depletion allowance affords a direct and simple means of ascertaining the allowable deduction. The taxpayer may know definitely his tax liability when the return is filed, a distinct advantage over the existing system under which delay and uncertainty have been the rule rather than the exception.

Under the proposed amendment, both the Government and the taxpayer may readily compute the amount of tax due at the time the return is filed. The taxpayer may proceed with his financial commitments and the further development of his mines without the fear of large additional assessments. He would rather pay more tax, as he will in some cases under this system, and know that his obligation is fully and definitely discharged, than to pay less tax after a long delay.



The proposed amendment provides a simple, definite method, easy of application that permits the prompt and final determination of the tax liability.

(2) Simplification.

*The phrase "gross income from the property" is used in existing statute, and, if applied in accordance with the trade practice of the different branches of the mining industry, has a definite, fixed meaning that is well understood in the industry. Fifteen per cent of the gross income from the property is accordingly an amount easily and definitely ascertainable. It affords in a simple, direct manner the amount of the allowable depletion deduction, and the prompt and final determination of net taxable income. [Italics supplied.]*

Therefore, although the valuation basis for computing depletion allowances is essentially sound, it is desirable to provide a short method in the interests of simplification.

The proposed amendment bases the deduction upon a percentage of gross income from the property, a measure that is simplicity itself—15 per cent of gross income.

(3) Economy of Administration.

The preparation and audit of returns of income in the metal mining industry have proven most expensive to both Government and taxpayer.

[511] (4) The Removal of Present Uncertainties.

(5) The Avoidance of Discrimination.

A group of taxpayers discriminated against at present embraces a large number of small operators, who make discoveries, but who are without organizations skilled in the procedure to be followed in proving



their discoveries. Such taxpayers are forced to employ expert assistance or else forego their rights under the law. Doubtless in many of these cases the expense involved in the employment of expert assistance would largely, if not entirely, offset the benefit derived from the establishment of discovery values. Under the percentage plan the small operator would in practice as well as in theory receive the same treatment as the large corporation, and without the expense and delays incident to the requirements of the Bureau of Internal Revenue in the administration of the present discovery provision.

The adoption of this plan would also remove the discrimination now existing against the mining industry as compared with the oil and gas industry.

#### GENERAL COMMENTS

It is quite generally understood that the percentage method of computing depletion has proven satisfactory to both Government and taxpayer in the Dominion of Canada.

From a careful survey of the data submitted, pursuant to requests of the Commissioner of Internal Revenue, to the Joint Committee on Internal Revenue Taxation, it is believed that the effect of the proposed amendment upon the Government revenue will not be adverse.

Since the percentage proposed is based upon an actual average of past allowances, it is believed that the total amount of tax paid by the industry will not be materially affected. Some reduction may be brought about through the granting of percentage depletion allowances to the many small operators who, because of the technicalities and difficulties in administration of the present discovery clause, have not been able to obtain their rights under the present law; but

while the number of such operators is large, their aggregate depletion allowance would be comparatively small in amount and it is believed that such allowance would not be greater than they are entitled to under present discovery provisions in the law.

[512] With respect to valuations prior to the date of the act, these certainly should be retained.

It is understood from part 2 of volume 1, division of investigation, reports of the Joint Committee on Internal Revenue Taxation, that percentage depletion in the oil and gas industries has proven satisfactory to the Government and has afforded a deduction that very closely approximates that formerly allowed under the valuation method. The proposed amendment will, it is confidently believed, afford equally satisfactory results in the metal-mining industry.

It is the general belief of the metal-mining industry that the amendment herewith proposed presents a simple workable, businesslike method of meeting the situation, which is fair to the Government and to the taxpayer. It is respectfully urged that it be enacted into law at the forthcoming session of Congress.

Respectfully submitted.

THE AMERICAN MINING CONGRESS,

J. F. CALLBREATH, *Secretary,*

McKINLEY W. KRIEGER,

*Chief, Tax Division.*

House Debate, 1927

(69 Cong. Record (Part 1), 70th Cong., 1st Sess.)

[599] The CHAIRMAN. The House is in Committee of the Whole House on the state of the Union for the further consideration of the bill H.R. 1, which the Clerk will report by title.

The Clerk read as follows:

A bill (H.R. 1) to reduce and equalize taxation, provide revenue, and for other purposes.

Mr. GREEN of Iowa. Mr. Chairman, under the order of the House the committee was permitted to return to page 79 for the purpose of considering the amendment offered by Mr. Arentz, and I believe he has the floor.

Mr. ARENTZ. Will the Clerk report the amendment?

The CHAIRMAN. Without objection, the Clerk will report the amendment.

The Clerk again reported the amendment, as follows:

Amendment offered by Mr. Arentz: On page 79, after line 24, add the following words: "This paragraph shall not apply to metal mines discovered after approval of this act," and add a new paragraph, as follows:

In the case of metal mines the allowance for depletion shall be 15 per cent of the gross income from the property during the taxable year. Such allowance shall not exceed 50 per cent of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.

Mr. ARENTZ. *Mr. Chairman, this amendment is introduced in the interest of simplification of the income tax. [Italics supplied.]*

One of the most technical and involved sections of the revenue bill is that one relating to depletion allowances.

No two men working independently of each other would reach, except by mere chance, the same conclusions regarding the rate of depletion to be applied to a particular ore or mineral deposit.

This is true in most cases where a technical physical examination is made of a natural resource developed but partially by underground workings or drill holes, irregular in shape, variable in mineral content, which in itself varies in price, to mention but a few of the factors entering into the determination of depletion allowance.

In the case of the United States against Ludey, Justice Brandeis had the following to say, as noted in Official Reports of the Supreme Court, under date of May 16, 1927:

*The amendment I have offered is in the interest of simplification. [Italics supplied.]*

It will be observed that the amendment proposed is a simple one which does not directly affect other provisions of the revenue act. Its adoption, therefore, will not make necessary any change in other portions of the act.

The outstanding advantages of the amendment are that without materially affecting the public revenue it provides a *simple, equitable, and definite method of computing the depletion allowance* that permits of the prompt and final determination of tax liability. It eliminates for the future the analytical appraisal of metal mines with attendant technical complexities. It means a great saving of expense to the Government as well as the taxpayer. [Italics supplied.]

[600] During this year, 1927, a questionnaire was sent to metal mining taxpayers throughout the country by the Commissioner of Internal Revenue with a letter stating that the joint committee had requested certain information regarding depletion allowances. In order to expedite the preparation of the information desired by the joint committee, the industry co-



operated almost 100 per cent and supplied all the information requested.

I have been informed by the Treasury Department that an investigation of the average depletion percentage allowed was found to be  $16\frac{1}{2}$  per cent on all returns allowed during the last four or five years.

Under the proposed amendment both the Government and the taxpayer may readily compute the amount of tax due at the time the return is filed. The taxpayer may proceed with his financial commitments and the further development of his mines without fear of large additional assessments. He would rather pay more tax, as he will in some cases under this system, and know that his obligation is fully and definitely discharged than to pay less tax after long delay.

The preparation and audit returns of income in the metal-mining industry have proven most expensive to both Government and taxpayer.

In the introduction of this amendment it is my desire to prevent this.

For the future discovery may be eliminated upon the adoption of an adequate percentage basis as proposed in this amendment. [Applause.]

Mr. COLTON. Is it not intended by the gentleman's amendment to give to the metal mines, as far as possible, a definite per cent for depletion the same as is now extended to oil companies? This would result in being helpful to the Government as well as to the mining industry, would it not?

Mr. ARENTZ. I will say to the Chairman of the committee that it is not my intention to press this amendment at this time, but I would like to receive from the chairman of this great committee, the Committee on



*Ways and Means, a statement as to the extent of his desires to cooperate to the end that this elimination of difficulty of arriving at a return may be had by the introduction of amendments offered to it. [Italics supplied.]*

Mr. GREEN of Iowa. Well, in answer to the inquiry of the gentleman, I think the gentleman has acted very fairly about it. He says he does not intend to press the adoption of the amendment at this time. The circumstances are these, as indicated by the remarks which the gentleman read from an article I wrote for the Saturday Evening Post. I think something ought to be done along this line, and it would undoubtedly, as the gentleman says, greatly simplify a matter that has caused the department a great deal of difficulty and trouble; and unfortunately in our discussions in the committee we took so much time with other matters that we got to this the last thing, and we did not have time properly to consider it. Not only that, but the experts never had time to be sure they knew what kind of an amendment ought to be prepared. Now, in pursuance of what the gentleman says, let the matter go over to the Senate and I am sure the mining interests will be taken care of over there, and by the time we get there we can tell what kind of a provision ought to be inserted; and if the Senate puts it in, as far as I am personally concerned, I will be very sympathetic with it.

Mr. ARENTZ. The idea with me is that the committee should not stand against this amendment simply because the experts might stand for something defining gross income, or something of that kind. When you talk of copper mines, for example, the definition is different from that when you talk of gold and silver mines and of lead-zinc mines. I hope you will not

hesitate in accepting this very important provision to clarify a subject which has been burdensome to taxpayer and Government alike for years and has resulted in much litigation, misunderstanding, and expense for the reasons I have stated. I thank the chairman for his courtesy and the sympathetic interest he has shown in this amendment.

Mr. GREEN of Iowa. We simply want time to go into this matter. I think at present the amendment ought to be voted down.

Mr. ARENTZ. Mr. Chairman, I withdraw my amendment.

\* \* \* \* \*

*Senate Hearings, 1928*

(Revenue Act of 1928, Hearings before the Committee on Finance, United States Senate, 70th Cong., 1st Sess., on H.R. 1.)

[303]

\* \* \* \* \*

The CHAIRMAN. I have also a brief on section 114-B, *in behalf of the metal-mining industry of the United States, submitted by the American Mining Congress, as well as a memorandum in relation to the brief. They will all go into the record at this point. [Italics supplied.]*

(The statements referred to are as follows:)

[304] Statement in behalf of the Metal Mining Industry of the United States.

*March 23, 1928.*

*To the honorable chairman and members of the Committee on Finance in the Senate of the United States:*

GENTLEMEN. At a hearing held on November 4, 1927, before the Committee on Ways and Means of the United States House of Representatives, on the pro-

posed revision of the revenue act of 1926, the American Mining Congress, representing the operators of metal mines of this country, proposed the following amendment to section 204(c) of the revenue act of 1926 to be incorporated in the proposed revenue bill for 1928:

\* \* \* \* \*

[For text of amendment, see House Hearings, 1927-1928, *supra*, pp. 42-43.]

NOTE.—The above amendment in italics would be added to section 114, H.R. 1 on page 79, after line 24.

It will be noted that the language of the proposed new paragraph as to metal mines follows that of the provision relating to depletion of oil wells which has been said to be satisfactory.

#### HISTORY OF PROPOSAL

When the 1926 revenue bill was being considered in the conference committee of the House and Senate, on or about February 15, 1926, it was reported that a percentage-of-income basis for depletion of mines was being considered. As the bill was to be agreed upon by the conference committee within a period of four or five days from that time, representatives of the American Mining Congress advised members of the conference committee that it would be impossible for the industry, on such short notice, to prepare and consider the data necessary to an intelligent conclusion respecting any plan of this nature that might be proposed. It is understood that a report was made to the conference committee by a representative of the Treasury Department on or about [305] February 18, 1926, to the effect that it would be impracticable to provide in the 1926 bill for percentage depletion in the case of mines, as it would be impossible to determine within the time

available what percentage rate or rates should apply to different branches of the mining industry. Therefore no action was taken, but it was understood by those interested that the subject would be considered by the Joint Committee on Internal Revenue Taxation created by the revenue act of 1926.

Shortly after the organization of the joint committee in 1926, an announcement was issued from the office of that committee that depletion would be one of the first subjects taken up for study. During June, July, and August, 1927, a letter and questionnaire were sent to metal-mining taxpayers throughout the country by the Commissioner of Internal Revenue. The following are copies of letters received by the American Mining Congress showing the scope and purpose of the investigation of depletion allowances in the mining industry initiated by the Commissioner of Internal Revenue in order to comply with a request from the joint committee for information.

[306] In order to expedite the preparation by the bureau of the information desired by the joint committee, the metal-mining industry cooperated almost 100 per cent, and supplied all the information requested. It is understood the coal-mining industry cooperated in the same manner. In the meantime, believing that the matter was certain to be taken up in this Congress, and in order to render all possible assistance to the joint committee, and to other committees of Congress, and to arrive at a satisfactory solution of the question, numerous meetings were held in the metal-mining industry during August, September, October, November, and December, 1927, at which the subject was given thorough consideration by representatives of all branches of the metal-mining industry.

## CONCLUSIONS OF THE METAL-MINING INDUSTRY

As a result of the study made by the metal-mining industry, the conclusion was reached that the application of a percentage-of-income basis for the determination of depletion allowances in the case of metal mines is practicable. From the best information available to the industry, it was found that the average of depletion deductions in the case of metal mines allowed by the Treasury Department under existing law during the five years, 1922 to 1926, inclusive, was in excess of 15 per cent of gross income. Therefore, representatives of the metal-mining industry decided that 15 per cent of gross income would be a fair basis for the future, provided it shall be enacted and applied without abrogating or disturbing any basis already established or allowable under existing and prior acts.

\*       \*       \*       \*       \*

The provisions of existing and earlier revenue acts employing a basic date method of valuation for the computation of depletion are and always have been based on sound economic principles, and for lack of any experience as to means and results, it would have been unwise, if not impracticable, to have employed at the beginning any other method. None the less, it always has been desirable to reach the same result by a shorter and simpler method. And now as a result of a practical experience of more than a decade in computing depletion on a valuation basis, it has become possible to propose a definite rate of depletion for metal mines to govern in the future that will give assuredly a result fairly comparable to that obtained by valuation, and without disturbing those valuations already agreed upon with the Treasury Department. Because of this experience, the rate proposed has a background of statistical authority.



[307] INTERPRETATIONS OF PREVIOUS AND EXISTING DISCOVERY PROVISIONS OF THE REVENUE LAW

The effect of the discovery provision, had it been applied to all minerals discovered after March 1, 1913, would have been to allow as a deduction from gross income of the mine taxpayer the present value in place as of date of discovery of such mineral or that capital value which was property. In other words, Congress, by enacting the discovery provisions, recognized a fundamental right of private property in this country, that whatever of value is inherent therein belongs to the owner thereof and is his capital.

[308] CONFERENCES WITH THE TREASURY DEPARTMENT

Several conferences have been held with officials of the Treasury Department culminating in a general conference of February 1, 1928. Some questions had been raised by engineers of the department with respect to methods of arriving at the 15 per cent rate proposed. At this conference it was demonstrated that as to ores valued in the past by the department engineers, the rate of depletion in relation to gross income was in practically all cases in excess of 15 per cent.

It was contended by representatives of the mining industry that in determining what per cent of gross income should apply as a basis for the depletion allowance, only ores valued in the past should be taken into account. It is conceded by all who are familiar with the depletion question that if ore reserves could have been accurately determined in all cases, as they have been in some, the taxpayer would receive the depletion allowance on every unit produced until the mine is exhausted. Inasmuch as it has been impossible to ac-

curately estimate ore reserves in all cases, it is only fair that the statistical background we now have should be used in providing for a fair allowance representing the value of the mineral in place on a percentage of gross income basis.

The 15 per cent of gross income proposed merely means that 15 cents out of each dollar received from the sale of ore represents what has been determined in the past to be a conservative approximation of the present worth as of the basic date of ore in place. While this amount is somewhat lower than the average for ores valued in the past, the mining industry has agreed that it will be a satisfactory basis to apply to new ores developed or discovered in the future, and it eliminates the necessity for estimating tonnage to be valued.

These arguments are supported by the Supreme Court of the United States in the case of United States v. Ludey, decided May 16, 1927. \* \* \*

[309] It is believed that officials of the Treasury Department are satisfied that the 15 per cent rate proposed is reasonable as a basis for depletion allowances in the case of all metals. As the result of these conferences with the Treasury, we are of the opinion that little question will be raised by the department concerning the matter of the rate. The real issue that will be presented to your honorable committee will be the question of how the percentage plan is to be applied, if adopted.

#### APPLICATION OF THE PERCENTAGE PLAN

[310] However, the mining industry is willing to accept the 15 per cent of gross-income basis for depletion allowances as a substitute for discovery value in the case of discoveries made after the approval of this act. The mining industry also contends that the per-

centage plan should be adapted to the situation in such a manner as to automatically correct underestimates of ore reserves; that is, where in prior valuations the estimates of ore reserves are clearly inadequate and the taxpayer has discovered and developed new tonnage, the percentage basis should apply to such tonnage irrespective of whether or not he would be entitled to discovery value on such tonnage under the existing rules and regulations of the department. In other words, the mining industry urges that the percentage plan be applied as the discovery provision should have been applied—to entitle the taxpayer to the “reasonable allowance for depletion” on the entire mineral contents of his mine.

FIFTEEN CENTS OUT OF EACH DOLLAR RECEIVED FROM THE SALE OF ORE BECOMES THE FIXED VALUATION OF ALL ORES NOT PREVIOUSLY VALUED

This precludes future errors in valuation such as underestimates of tonnage and errors of judgment in the application of the various factors involved in estimating the present worth of such tonnage as of a basic date, and avoids the enormous expense entailed by both taxpayer and Government in making valuations. We believe the statistical compilations made by the department and the Joint Committee on Internal Revenue Taxation with respect to ores valued in the past will show conclusively that *15 cents out of each dollar received from the sale of ore* is less than the average depletion allowance, not only in the case of each metal, but as to all metals averaged together. [Italics supplied.]

The percentage plan proposed unquestionably will be simple of administration, and will tend to equalize conditions as between different taxpayers in the metal-mining industry.

## EFFECT UPON REVENUE

Under this percentage plan in all cases where the metal-mining taxpayer has an operating profit the Government will derive a tax, since, no matter how small the profit, at least 50 percent of the net income, before deducting depletion, will be subject to tax. This plan embodies a double limitation that is advantageous to the Government; first, in the case of high profits the maximum allowance is limited to 15 percent of gross income; second, in the case of low profits the maximum is 50 percent of net income. Thus, so long as mines make any operating profits the Government will derive a continuous revenue therefrom.

Respectfully submitted.

McKINLEY W. KRIEGER,  
*Chief Tax Division,*  
*The American Mining Congress.*

## [311] ADDENDA

EXTRACTS FROM AMERICAN MINING CONGRESS BRIEF  
 FILED WITH THE SENATE COMMITTEE ON FINANCE, 1926.

## HISTORY OF THE DEPLETION PROVISIONS

[312-313] Let us turn from the legislative history of depletion to its economic base and justification.

DEPLETION BASED ON SOUND PRINCIPLES—THE MAINTENANCE OF A CAPITAL RESERVE BASED ON THE VALUE OF ORE OR MINERAL IN PLACE REPRESENTS A SOUND FINANCIAL PRINCIPLE, IS AN ECONOMIC NECESSITY TO THE CONTINUANCE OF THE INDUSTRY AND ITS RECOGNITION IN THE FEDERAL TAX LAWS IS FULLY JUSTIFIED.

[316] MEMORANDUM RELATIVE TO QUESTIONS RAISED BY  
DEPARTMENT OFFICIALS CONCERNING THE PROPOSED  
AMENDMENT TO THE REVENUE BILL TO PROVIDE FOR DE-  
PLETION OF METAL MINES ON A PERCENTAGE-OF-INCOME  
BASIS.

[317] 3. *Bases for application of the percentage rate.*—The Treasury may say that the proposed amendment is not sufficiently specific in its language to furnish a definite basis for determination of the amounts to which the 15 per cent and the 50 per cent are to be applied.

*Answer: The determination of 15 per cent as a fair average rate applicable to the different divisions of the metal mining industry took into account the various practices which were customary within each division in disposing of ores, concentrates, or metals. The department seems to feel that the wording of the heretofore proposed amendment would not enable it to recognize these variations as to the different divisions of the industry. [Italics supplied.]*

*To meet this objection, the changed wording set forth in the revised form of the amendment submitted herewith is suggested. With this wording and the general power which the commissioner has under the law to prescribe regulations, it is believed all requirements are met. [Italics supplied.]*

*Attention is called to the fact that certain mining companies do not actually dispose of their products in the open market, but transfer them to related or affiliated companies on a cost-plus or other intercompany basis. Authority probably is necessary in the law to allow the commissioner properly to deal with such situations and the last sentence of the suggested revised amendment covers these situations. [Italics supplied.]*



## PROPOSED AMENDMENT AS NOW REVISED

Add to section 114, H.R. 1, page 79, after line 24, the following:

This paragraph shall not apply to metal mines discovered after the approval of this act.

And add a new paragraph, as follows:

(3) In the case of metal mines, if as to any ores or metals no depletion is allowable under the preceding paragraphs, or if the taxpayer shall waive as to any property for the taxable year and all subsequent years the right to any depletion allowance under the preceding paragraphs, the depletion allowance shall be 15 per centum of the total receipts from the sale or other disposition of the ores or metals from the property during the taxable year. Such allowance shall not exceed 50 per centum of the net income (computed without allowance for depletion) from the property. *Where products are transferred on an intercompany basis at a price greater or less than the market value, the total receipts and the net income subject to the percentage depletion reduction shall be constructively computed on the basis of current market value for the product so transferred. [Italics supplied.]*

[361-362] Statement of HARRY L. GANDY, executive secretary of the National Coal Association, Washington, D.C.

Mr. GANDY. Mr. Chairman and gentlemen of the committee, I am executive secretary of the National Coal Association, a nation-wide association of bituminous coal operators.

The suggestion has been made, in which the National Coal Association heartily concurs, that it may be the part of wisdom by this committee to confine

this bill to the matter of rates and noncontroversial questions.

Senator Watson's amendment offered to this bill would simply take the wording of section 204(c)(2), being the oil and gas optional standard rate for depletion, and strike out the words "oil and gas" and insert the words "coal mines" and change the rate from 27½ per cent of gross return to 6 per cent. It is barely possible that in the discussion of that amendment in the committee you may want to change it some.

The CHAIRMAN. There has already been suggested by the American Mining Congress an amendment to bring about the same result. But it was not 6 per cent, but 15 per cent.

Mr. GANDY. That applies to metal mines, and this is the same proposition applying to coal mines.

The CHAIRMAN. You may just put in your amendment at this time. We will take them all up at once.

Mr. GANDY. It is as follows:

In the case of coal mines the allowance for depletion shall be 6 per centum of the gross income from the property during the taxable year. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph. That is all, Mr. Chairman.

Revenue Act of 1928

(c. 852, 45 Stat. 791, 799, 821)

### SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(1) *Depletion*.—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. In the case of leases the deduction shall be equitably apportioned between the lessor and lessee. \* \* \* [For percentage depletion in case of oil and gas wells, see Section 114(b)(3).]

(m) *Basis for depreciation and depletion*.—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114.

#### SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(b) *Basis for depletion*.—

(1) *General rule*.—The basis upon which depletion is to be allowed in respect of any property shall be the same as is provided in section 113 for the purpose of determining the gain or loss upon the sale or other disposition of such property, except as provided in paragraphs (2) and (3) of this subsection.

(2) *Discovery value in case of mines*. \* \* \*

(3) *Percentage depletion for oil and gas wells*.—In the case of oil and gas wells the allowance for depletion shall be  $27\frac{1}{2}$  per centum of the gross income from the property during the taxable year. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.

(1929 ed.)

**ART. 221. Depletion of mines, oil and gas wells; depreciation of improvements.—** \* \* \*

When used in these articles (221-257) covering depletion and depreciation—

(i) "Depletion allowance based on the income from oil and gas wells": The deduction for depletion based on the income from oil and gas wells shall not exceed 50 per cent of the net income of the taxpayer, computed without allowance for depletion, from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to the income from the property. The phrase "net income of the taxpayer (computed without allowance for depletion)" means *the gross income from the sale of oil and gas less the deductions in respect to the property upon which depletion is claimed, including overhead and operating expenses, development expenses (if the taxpayer has elected to deduct development expenses), depreciation, taxes, losses sustained, etc., but excluding any allowance for depletion. If the oil and gas are not sold on the property but are manufactured or converted into a refined product or are transported from the property prior to sale, then the gross income shall be assumed to be equivalent to the market or field price of the oil and gas before conversion or transportation.* Depreciation, taxes, and such expenses as overhead (which can not be directly attributed to any particular property) shall be allocated on the basis of the ratio of the number of units produced from the property on which depletion is claimed to the total number of units produced from

the operating division in which the property is located. In cases where the taxpayer, in addition to producing oil and gas, engages in additional activities such as operating refineries and transportation lines, depreciation, taxes, and such expenses as overhead which can not be directly attributed to any specific activity, shall be allocated to the production of oil and gas on the basis of the ratio which the operating expenses and development expenses (if the taxpayer has elected to deduct development expenses) directly attributable to the production of oil and gas bear to the taxpayer's total operating expenses and development expenses. [Italics supplied.]

ART. 241. *Depletion in the case of oil and gas wells.*—Under section 114(b)(3), in the case of oil and gas wells, a taxpayer may deduct for depletion an amount equal to  $27\frac{1}{2}$  per cent of the gross income from the property during the taxable year, but such deduction shall not exceed 50 per cent of the net income of the taxpayer (computed without allowance for depletion) from the property. (See article 221 (i).) In no case shall the deduction computed under this paragraph be less than it would be if computed upon the basis of the cost of the property or its value at the basic date, as the case may be. In general, "the property," as the term is used in section 114(b)(3) and this article, refers to the separate tracts or leases of the taxpayer.

1930

[The Joint Committee on Internal Revenue Taxation made a preliminary report on depletion in relation to *metal mines*, based upon surveys conducted by the Treasury Department, which included statistics, a proposal and brief submitted by the American Mining Congress, and a report (commonly called the Shepherd Report) which was made by a mining engineer of the



Joint Committee and which commented favorably upon the proposal of the American Mining Congress. Joint Committee hearings were also held after the Joint Committee's preliminary report.]

**Joint Committee Report, 1930**

(Preliminary Report on Depletion, Report to the Joint Committee on Internal Revenue Taxation from its staff (1930), Vol. 1, Part 8.)

**LETTER OF SUBMITTAL**

**CONGRESS OF THE UNITED STATES  
JOINT COMMITTEE ON INTERNAL REVENUE TAXATION**

*WASHINGTON, September 17, 1929.*

**HON. WILLIS C. HAWLEY,**  
*Chairman Joint Committee on Internal Revenue Taxation,*  
*Washington, D.C.*

**MY DEAR CHAIRMAN.** There is submitted herewith a preliminary report on depletion.

In my opinion, the report is sufficient to establish, first, that the distribution of depletion allowances among the taxpayers in the mining and quarrying industry is inequitable; second, that in certain cases the allowances are excessive; and third, that the present system lacks certainty and is expensive to both Government and taxpayer.

The present depletion allowances depend in each case almost entirely upon certain factors and conditions which would appear to have very little, if any, relationship to the computation of a fair annual income at the present time. In fact, in proposing two new plans for the determination of depletion, the point of view has been taken that it is most important to have taxpayers similarly situated pay the same rate of tax so that they may compete with each other without

disadvantage as far as Federal taxes are concerned. Under the present system some taxpayers pay high taxes and others are practically tax exempt.

The methods of percentage depletion proposed for consideration are not such a departure from the present system as would appear from a preliminary inspection. The analytic method of valuation now used in most important cases arrives at a value through the estimation of future expected profits. Depletion based on a percentage of the net income from the property merely uses actual figures instead of estimated figures.

While this report does not cover the subject completely, it is hoped that it will form a basis for discussion. Statistics which would appear helpful to those desiring to make a further study of this subject are included in the appendix. It is recommended that the report be published in order that it may be available for public examination and analysis.

Very respectfully.

L. H. PARKER, *Chief of Staff.*

## [1] PRELIMINARY REPORT ON DEPLETION

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### FOREWORD

The valuation of all natural resources for depletion purposes has been required under every revenue act since 1916, with the exception of relatively few cases in which depletion is based on the cash actually paid for the property. The difficulties confronting the Bureau of Internal Revenue in the valuation of natural resources are almost insurmountable. Various causes may be assigned for this. In the first place, the methods of valuation adopted permit of wide discretion in individual judgment. The result is differ-

ences of opinion even with respect to the same properties. Many actual cases exist in which experienced engineers have differed in their reports on the same property by at least 400 per cent. In the second place, the date of valuation is so far removed from the date as of which the examination must be made that it is practically impossible to secure sufficient evidence to determine a correct valuation. In the third place, the turnover of personnel and the magnitude of the undertaking have added to the difficulties.

This report first considers the operation and effect of the depletion provisions of the existing law, with special reference to the resulting inequalities. A plan for percentage depletion which will eliminate, at least partially, the difficulties and inequities arising under the present system is next discussed. The subject is presented in as simple language as its technical nature will permit. The data necessary to support various statements and conclusions are in the appendix, together with other statistics which may be useful to those making further researches on this subject.

The primary purpose of the report is to form a basis for an intelligent discussion of the subject of depletion. It has been found impracticable to assemble sufficient data at this time to make a complete test of the soundness of the principles set forth. It is recommended that this preliminary report be printed for public examination and analysis so that taxpayers may have ample opportunity to analyze and apply these principles to their individual cases.

#### SYNOPSIS

##### 1. No Constitutional Limitation.

The Constitution does not require that the mine owner be given any allowance for depletion. The Supreme Court has held that this deduction is not one to

which he is entitled as a matter of right, but is a concession made by Congress in recognition of the equity in such cases.

## [2] 2. Accounting Theory.

From an accounting standpoint, the proper basis for determining depletion is the cost of the property. This basis is not recommended because of the apparent hardships resulting from its application.

## 3. Statutory Provisions.

The existing law provides for five different bases for determining depletion, namely: Cost; March 1, 1913, value; discovery value;  $27\frac{1}{2}$  per cent of gross income; and 50 per cent of net income.

## 4. Methods of Valuation in Use by the Bureau.

The methods of valuation employed by the Bureau of Internal Revenue are as follows: (a) Comparative sales method, (b) prevailing royalty method, and (c) analytic appraisal method. As each of these methods is based upon different principles, it necessarily follows that the same results are not obtained.

## 5. Defects in the Present System.

(a) *Administrative.* — The administrative defects under the present system are (1) lack of uniformity in computing depletion, due to the exercise of individual judgment; (2) lapse of time between the basic date and the examination of the return; (3) inability to secure sufficient evidence to establish a correct valuation; and (4) excessive expense to both Government and taxpayer.

(b) *Instability of revenue.* — Under the present system, the depletion deduction is allowed before arriving at net income. In lean years the present depletion allowances practically wipe out the tax of this industry,

in spite of the fact that substantial dividends are paid. On the other hand, in prosperous years high taxes are collected. As a result, the revenue received from the industry as a whole is more unstable than in the case of the other industries. This appears undesirable from a practical revenue standpoint.

(c) *Inequitable results.*—There are many inequitable results in the present system. The different laws relating to depletion as applied to the different industries are not uniform. The oil and gas industry is allowed percentage depletion based upon gross income before the depletion deduction is computed. The effect of this allowance is to vary the deduction in proportion to the gross receipts from the sale of these products. Contrasted with this are the allowances based on a March 1, 1913, or a discovery value, in which cases the depletion varies with the quantity produced. Finally, in certain limiting cases, depletion is allowed on the basis of a percentage of the net income from the property. The valuation methods applied by both the Bureau of Internal Revenue and the taxpayer are not uniform and produce many inequalities between different industries. Valuations by the widely used analytic appraisal method depend largely on the peculiar conditions existing as of the basic date. These peculiar conditions appear to have little to do with an equitable tax on annual income. For example, taxpayers who make discoveries in periods of prosperity are allowed large deductions for depletion; whereas those who are so unfortunate as to make discoveries in years of depression are required throughout the life of the property to take a lower rate.

## 6. Methods Proposed for Consideration.

*Several methods for computing depletion are proposed for consideration. They are as follows: (a) Fixed rate per unit method, [3]. (b) percentage of*



*gross income method, and (c) depletion based on percentage of net income, consisting of plans (1) and (2).* Both the fixed rate per unit method and the percentage of gross income method involve a wide departure from the allowance authorized by existing law and appear to produce inequities in the case of certain industries. Plan No. (1) of the percentage of net income method is based upon a percentage of net income from the property and is similar to the method adopted by Canada. Plan No. (2) is based upon a percentage of net income adjusted so as to allocate a reasonable amount of such net income to plant investment. This last plan when applied to concrete cases appears to produce more equitable results than the first plan. [Italics supplied.]

#### 7. Advantages of Percentage of Net Income Method.

The percentage of net income method has many advantages. It will result in (a) elimination of discovery depletion, (b) simplification of administration, (c) partial elimination of March 1, 1913, valuations, (d) stability of revenue from this source, and (e) correction of inequities between different industries as well as between taxpayers in the same industry.

#### [6] Defects in the Present System.

(a) *Administrative difficulties.*—One of the principal administrative defects in the present system is the lack of uniformity and certainty in computing depletion. It is axiomatic that formulæ and methods involving different basic principles do not produce the same results. Each of the three methods of valuation in use by the Bureau of Internal Revenue involves basic principles not found in the other two methods. The application, therefore, of these methods must, of necessity, result in different values. \* \* \*

[8] (c) *Inequitable results.*—One test of a satisfactory system of taxation is whether or not it imposes a uniform burden upon all industries. \* \* \*

[12] *The present system may result in gross inequities between individual taxpayers within the same branch of the mining industry.* \* \* \* The two companies occupy adjoining properties, they are competitors in the open market, and apparently are operating under similar conditions. The unit rate of depletion, however, for the one is double that of the other. [Italics supplied.]

#### Methods Proposed for Consideration.

Inasmuch as the present system of depletion has been shown to be neither simple in its application nor equitable in its results, it is desirable to find a substitute for this system. Several methods have been proposed and considered, each one of which will be discussed.

(a) Fixed rate per unit method.— \* \* \*

[13] (b) *Percentage of gross income method.*—The second method proposed for consideration is a form of percentage depletion and was proposed in a brief submitted to the Ways and Means Committee when it was considering the revenue bill of 1928. (See Exhibit XXX.) This proposal, showing the changes, is as follows:

[The amendment is that which was proposed by the American Mining Congress, printed *supra*, pp. 42-43.]

[14] A report based on similar principles was submitted by Alex R. Shepherd, mining engineer for the

joint committee. This report is made a part of the appendix as Exhibit XXXI.

The method proposed by the American Mining Congress does not seem to meet the requirements as to uniformity of tax burden which have been discussed in this report. The method consists in applying a rate of 15 per cent to the gross income from the property in determining depletion. The percentage is arrived at from the average of the depletion allowed on cost, March 1, 1913, or discovery value. As this method is only effective in increasing the tax in the case of future discoveries, an apparent reduction in revenue to the Government from mining properties would follow its adoption. From the standpoint of simplicity, the method also appears to be undesirable. It still retains March 1, 1913, value and eliminates discovery value only with respect to the future. It also allows the metal-mining industry a still greater advantage than that received under the existing law. Under the existing law depletion is allowed only up to an amount equal to the cost, March 1, 1913, value, or discovery value, as the case may be, whereas the proposed method places no limit on the total depletion allowances except the practical limit set up by the exhaustion of the mine.

(c) *Depletion based on percentage of net income.*—

A third method which possesses considerable merit is to allow depletion based upon net income from the property. Such a method appears practicable in two forms. Plan No. 1 consists of a deduction for depletion based upon a percentage of the net income from the property. Plan No. 2 consists in allowing depletion based upon the net income from the property after a reasonable amount of the net income has been allocated to the plant investment.

[22]

## CONCLUDING REMARKS

This report shows that the present system for determining depletion is neither simple in its application nor equitable in its results. The present system is not only inequitable between taxpayers in the same branch of the mining and quarrying industry, but the distribution between the different branches is unjust. For example, bituminous coal mine operators have not received the relief given other mine operators. The coal industry has been profitable only in a few years and is now in a condition as depressed as agriculture. The present system results in taking away from the bituminous coal industry a large proportion of its profits in taxes in the infrequent year of prosperity. It appears, therefore, that a substitute method is desirable.

This report proposes several substitute methods for discussion. While the report indicates a preference for plan No. 2, a method of percentage depletion based on the net income from the property, it is hoped that the other methods will also receive careful analysis. In order to limit the scope of the discussion to the determination of a sound general method, certain subsidiary propositions like net losses, distribution of depletion between lessor and lessee, etc., are not considered. If a sound method can be devised, the related minor problems can readily be solved.

It is believed that if any plan of computing depletion is adopted based on a percentage of net income from the property, that both March 1, 1913, depletion and discovery depletion should be eliminated if substantial simplification is to result. It should be added in this connection that the argument has been advanced that it will be exceedingly difficult to determine the net income from the property. This argu-

ment does not appear to be supported by actual facts.

The existing law, namely, section 114(b)(2) of the revenue act of 1928, requires such a determination by providing that the allowance for discovery value in the case of mines *shall not exceed 50 per cent of the net income of the taxpayer from the property. Limitations of somewhat similar character are contained in the revenue acts of 1921, 1924, and 1926. During the many years that this requirement has been in the law, no complaint has been made that the net income [p. 23] from the property could not be determined. Furthermore, many operators of mining companies admit that the method of bookkeeping employed by mining companies will show the net income from this source without difficulty. (Italics supplied.)*

Sufficient data is not available for fully testing the operation and effect of the methods proposed. It is hoped that this report will stimulate such interest in the subject that the Bureau of Internal Revenue, as well as the taxpayers affected, will make a thorough test of these methods by applying them to actual conditions.

Respectfully submitted.

L. H. PARKER, *Chief of Staff.*

[57]

## APPENDIX XXX

IN THE MATTER OF THE HEARING BEFORE THE COMMITTEE ON WAYS AND MEANS OF THE UNITED STATES HOUSE OF REPRESENTATIVES, SEVENTH CONGRESS, FIRST SESSION, ON THE PROPOSED REVISION OF THE REVENUE ACT OF 1926.

[Here follows the brief of the American Mining Congress, portions of which are printed *supra*, pp. 39-47.]



[63]

## APPENDIX XXXI

## SUMMARY REPORT ON DEPLETION OF METAL MINES

[Commonly called the Shepherd Report]

Mr. L. H. PARKER,

*Chief Division of Investigation,**Joint Committee on Internal Revenue Taxation.*

My DEAR MR. PARKER. Several months have been spent in the study of this subject. It has resulted in definitely determining in dollars and cents the average depletion allowances per unit (pounds, tons, etc.,) for the minerals produced, to the taxpayers engaged in the metal mining industry.

Figures have also been assembled to show the relation between the average depletion allowances to gross and net income from the metal mining properties, on the basis of percentages, with the object of simplification in enacting future legislation on this subject.

The work has been accomplished in cooperation with officials of the Treasury Department and the taxpayers, who have furnished the necessary figures. The tabulations submitted represent approximately 75 per cent of the total production of the industries. It is thought that this percentage of production fully covers those taxpayers reporting net income to the Treasury Department.

From the information received, it appears that both the Bureau of Internal Revenue and the taxpayers are favorably inclined to the percentage basis for depletion allowances, in lieu of the existing discovery provisions, not because substantially greater or less depletion will be allowed but because of simplicity and certainty in tax determination.

It is believed that the substitution of the percentage basis, in lieu of the present discovery clause, will re-

sult in definite and prompt settlement of tax liability, in simplification, and in economy, both for the Treasury Department and the taxpayers and in elimination of uncertainty and discrimination which exists at present. This matter has been brought to the attention of the Committee on Ways and Means at its recent hearings by the American Mining Congress, representing 75 per cent of the metal-mining producers.

From long experience in the industry and knowledge of the actual functioning of the revenue legislation during the past seven years, I personally believe the proposed percentage basis for depletion allowances is sound and should not reduce the revenue derived by the Government from the metal-mining industries. It should, over a period of years, increase the revenue.

For brevity and simplification, the subjects have been segregated under the following headings:

Part 1. Brief review of depletion and its relation to this industry today.

Part 2. Summary and results in the study of percentage depletion.

Part 3. Recommendations as to a reasonable rate for percentage depletion.

Part 4. Effect of the proposed legislation on the present and future revenue to the Government.

[64] Part 5. Remarks on the amendment to section 204(c) as proposed in brief submitted by the American Mining Congress to the Committee on Ways and Means.

Part 6. Practical application of percentage depletion method to various classes of metal mines.

Detailed tabulations of the statistics are available in case they are desired.

Respectfully submitted.

ALEX. R. SHEPHERD,  
Mining Engineer.

Part 1. Brief review on the subject of depletion and its relation to this industry today.

The depletion allowance as a deduction to the taxpayers is the return to him of that portion of the established value of his property which has been exhausted in any particular year.

From the standpoint of Federal taxation for the future there is no valid reason for the continuation of the valuation of the taxpayer's individual developments of new ore reserves in the natural course of his mining operations. It should be of no interest to the Government from what hole in the ground the ores are from as long as it receives the right amount of tax from the taxpayers.

Less than one-tenth of the total number of taxpayers in the metal mining industries produce over 50 per cent of the total production and doubtless pay their proportion of the taxes to the Government. *These large corporations operate many properties of their own and are completely equipped with treatment plants from one end of the country to the other. They further purchase, refine, and market the greater part of the metals produced by the other operators.* [Italics supplied.]

[65]

Part 2. Summary of the results of the study of percentage depletion.

Reports by the joint committee's staff and the Treasury Department, on the percentage basis for

depletion which has been in force for over a year in the case of oil and gas, show that it has functioned satisfactorily both from economical and administrative viewpoints and without loss of revenue to the Government.

*A careful study of this method as applied to metal mines indicates that the same results will be attained in practice as in the case of oil and gas. [Italics supplied.]*

The attached Table 1 is compiled from individual figures submitted by the metal-mining taxpayers and represents 75 per cent of the total American-owned production. It covers operations for the past five years (1922-1926), with gross sales (corresponding to gross income from the mining properties) of \$2,437,921,266, with depletion allowances of \$417,536,743 (which are based on cost, March 1, 1913, and discovery valuations).

The average depletion allowed for all metals is approximately 17 per cent of the gross sales for this period. This percentage expressed in cents per pound and per ton of metal on the basis of average depletion allowances is shown in Table 2.

In considering this table it should be borne in mind that these results are based on prices and expected profits which do not represent present-day conditions and what appeared to be a correct valuation in a particular case under certain conditions may be out of line with the facts to-day.

**TABLE 1.—Summary of the metal industries for a 5-year period (1922–1926), showing the gross sales (equivalent to the gross income from the property), and depletion allowed (on the basis of cost, March 1, 1913, and discovery valuations) for the different metals. This tabulation represents approximately 75 per cent of the total American-owned production**

	Gross receipts on basis of net smelter returns or equivalent	Depletion allowed	Depletion to net smelter returns or equivalent
			Percent
Lead-zinc ores <sup>1</sup> .....	\$290,625,002	\$50,026,529	17.21
Iron ores <sup>2</sup> .....	670,014,899	118,872,541	17.74
Coppers.....	1,318,794,543	226,930,118	17.21
Complex ores <sup>3</sup> .....	109,371,077	13,773,497	12.60
Gold and Silver.....	44,660,068	7,567,224	16.94
Miscellaneous metals.....	4,455,647	366,584	8.23
<b>Total.....</b>	<b>2,457,921,266</b>	<b>417,536,743</b>	<b>17.127</b>

<sup>1</sup> Includes Idaho and its silver values.

<sup>2</sup> Includes Lake Superior and Alabama ores.

<sup>3</sup> Mixed lead, zinc, copper, silver, and gold.

**[66] TABLE 2.—Summary of average depletion, allowances (per pound, ton, etc.) to the various metals as established by past valuations (on the basis of cost, March 1, 1913, and discovery methods) and approximate percentage of production, with localities**

Metal	Location	Percent of total production	Average depletion unit allowed	Class of ores
Iron ores.....	Lake Superior ranges	75	56.31 cents per ton.....	Average all grades and interests.
Copper.....	United States, Canada, and South America	75	2.606 cents per pound.....	Do.
Lead.....	Southeast Missouri	30	0.7512 cent per pound.....	Lead ore only.
Do.....	Utah, Colorado and Nevada	28	0.808 cent per pound.....	Complex ores. <sup>1</sup>
Do.....	Idaho	20	1.112 cents per pound.....	Do.
Do.....	Joplin district	16	\$4.29 per ton.....	Concentrates, zinc predominate. <sup>2</sup>
Zinc.....	do	60	do.....	Concentrates with lead.
Do.....	Eastern	15	0.3529 cent per ton.....	Zinc ore only.

<sup>1</sup> Complex ores. The practice in most cases has been to establish the depletion allowance on the predominating metal, though there are other commercial recoverable metals included, such as zinc, silver, and, in some cases, gold and copper, arsenic, etc. The greater portion of the complex ores is so<sup>1</sup> direct to smelters and refineries either in the crude or partially refined form.

<sup>2</sup> This rate includes some rock tonnages. On the basis of a 60 percent zinc-lead concentrate the depletion allowed approximates \$7.28 per ton; this is equivalent to six-tenths of 1 cent per pound of the combined lead and zinc metals.

No attempt has been made to ascertain separate average depletion units for gold and silver, as the major production is derived from the copper, lead, and zinc ores. However, the individual properties show approximately the same percentage to gross sales.

**Part 3. Recommendations as to a reasonable rate for percentage depletion.**

Table 1 shows that the metal-mining industry has received in depletion allowances an average deduction equivalent to about 17 per cent of the gross sales.



*From the study of this subject it is believed that 15 per cent of the gross sales value with a 50 per cent limitation to net income, would be a reasonable rate to allow the metal-mining industry for the future. This reduction by 2 per cent of the actual figures shown in the summary is thought advisable to offset the continuing effect of the percentage depletion method. [Italics supplied.]*

The 15 per cent depletion allowance on gross sales is equivalent to a theoretical deduction of 30 per cent on net income. In actual operations the 30 per cent on net may vary 15 per cent above or below this figure, depending on the profits made by the particular operation.

[67]

Part 4. Effect of the proposed legislation on the present and future revenue to the Government

[68]. Part 5. Remarks of the amendment to section 204(c) as proposed by the American Mining Congress on behalf of the metal industry to the Committee on Ways and Means

It will be noted that the wording of the proposed amendment, section 204(c)(2) is identical with the 1926 act of oil and gas. If it functioned in a similar manner all past allowed and claimed discovery depletion would automatically be superseded by the percentage basis, with the enactment of the amendment.

However, on page 9, paragraph 5, it is stated "With respect to discoveries prior to date of the act, it is strongly felt that these should be retained." The reasons given follow in the brief.

The question as to the advisability of attempting to keep the discovery depletion allowances (allowed and claimed) for the future—is one upon which there seems to be a division of opinion among the taxpayers.

In whatever manner it is decided to handle the matter, there are other questions which will need consideration and final determination.

*It will be necessary to define what is meant by gross income from the property and to definitely indicate the point in accounting at which it is to be determined as well as other details. This can be done, either in the act, or interpreted in the regulations. [Italics supplied.]*

*The consensus of opinion seems to be that the act should be written as simply as possible (as in the case of oil and gas) and the necessary definitions should be written into the regulations. [Italics supplied.]*

[69]

Part 6. Practical application of percentage depletion method to various classes of metal mines.

In order that a better understanding may be had of the proposed plans for the determination of gross income from the property and net income, in reference to percentage depletion, a brief summary is given for each of the metals, showing the various metallurgical processes or steps through which they must pass from the crude mine ore to the marketable product.

The process of preparing copper, lead, zinc, silver, and gold for sale to a manufacturer usually entails five distinct operations.

1. Mining, or getting the metal-bearing rock out of the ground.

2. Concentrating, or separating the profitable portions of the run-of-the-mine rock from the unprofitable. This involves crushing, fine grinding, concentrating tables and in most cases to-day selective flotation of the remaining portion of the minerals in the rock. By these processes from 75 to 95 per cent of the valuable minerals are recovered from the crude ore and the bulk reduced from 10 to 30 tons of crude ore to 1 of concentrates. Five to twenty-five per cent of the metal remains in the crude ore and is lost or goes into the waste piles.

3. Smelting, or isolating the metallic constituents as impure bullion from the remainder as slag after melting the whole of the concentrate with appropriate fluxes in a suitable furnace.

4. Refining or separating the metals from each other.

5. Marketing the refined products.

There is a wide diversity in methods, practices, and application of these five operations depending on locality, metals, and expediency in many cases.

*However, for the present purposes it is not such a difficult matter to group the methods and practices and to demonstrate the point at which the sales of the products take place. Generally speaking, all the metals are sold by the producers on the basis of the market quotation of the refined product. [Italics supplied.]*

*In the case of the smaller operator, the product in most all cases is sold in the crude or semirefined (concentrate) state to smelter under contract or otherwise. [Italics supplied.]*

The smelting after weighing and sampling the ore or concentrate renders the seller a statement setting forth:

The gross metallic contents of the shipment.

Net metallic contents and market quotation.

Deduction for all costs, of freight, treatment, penalties, etc.

[70] *Net value in dollars and cents to seller (known as the net smelter returns) and a check in favor of seller for the product sold. Each ore shipment to the smelter is generally liquidated in the above manner. [Italics supplied.]*

*Therefore, in the case of 90 per cent (in numbers) of the taxpayers their gross income from the property is the smelter return settlement, less royalty due lessors. [Italics supplied.]*

*On the taxpayer's returns this figure forms the base for his (1) gross sales from trading, etc. His cost for fire treatment, losses in refining, freights and marketing have already been deducted. The remaining costs of mining, concentrating, overhead, interests, etc., are further to be deducted along the line. In actual practice, there appears to be some variation in reporting these credits and deductions but undoubtedly the net results are the same in most cases. [Italics supplied.]*

*In the case of the large mine operators with complete plants for concentrating, smelting, refining, and marketing, the practice in accounting from a tax-reporting standpoint is more or less the same as the smaller operator who sells to a smelter or its agent. [Italics supplied.]*

Most of them do custom work and therefore must keep accounts of the cost of refining ores from their own properties in a similar manner as is done with with purchases ores. *Therefore, the net smelter re-*

turn basis can apply equally to their own operations. [Italics supplied.]

*They will receive a slight advantage over the smaller operator in that he pays whatever profits the larger operator charges for treating and marketing the product and may get slightly less recovery than is actually made.* However, this is the case in all business transactions, and from a taxation standpoint we can only compute the tax on what a taxpayer actually receives for the products sold. [Italics supplied.]

A thorough survey of the situation shows that the metals are sold on different bases in the refined, semi-refined, and crude states. In order to clarify the matter, a brief review is herewith set forth for the different metals.

**Copper.**—The greater part of this metal is marketed in New York on the basis of the refined metal. The total mine production is around 2,500,000,000 pounds annually. Charts are available to show the sources and distribution of this metal which total approximately one-half of the value of all the metals produced.

There are about 40 leading producers of copper to-day. Of these, 12 companies produce 75 per cent of the entire production and of these 12, three corporations control 75 per cent of the output. In addition, they refine and market probably over 90 per cent of the total production of the United States, Canada and South America. It is, therefore, evident that their sales value must be computed on the basis of the refined metals, which also includes both gold and silver as byproducts.

**Lead and zinc.**—The total mine production of lead to-day is around 2,000,000,000 pounds of refined metal annually. The total mine production of zinc to-day



is around one and one-third billions pounds of refined metal.

Probably in over 70 per cent of this production the two metals are mined together (from complex ores), also with silver and a small amount of copper and gold in some localities, as by-products.

[71] Practically all of the metals require fire treatment and *are sold in the semirefined or concentrate basis to smelters or refineries*, and while practices vary in localities the basis of receipts for the product sold correspond to the "net smelter settlement." *This means that "gross income from the property" is definitely fixed at the mine or mill, as in the case of smelter settlement. While there are a few exceptions to this general state, there should be no difficulty in establishing the same mine or mill basis for them* [Italics supplied.]

*Gold and silver.*—Approximately two-thirds of the total production of these metals is produced as a by-product, in copper, lead, and zinc mining. The remaining third is produced by mines which either produce both metals together or singly. *In a few instances, pure bullion is produced at the property, in most instances the refining is done by smelters. In either case it is evident that their gross income from the property is logically based on the product sold or refined metal.* [Italics supplied.]

*Iron ores.*—Eighty per cent of the iron ore is produced from the Lake Superior regions. This ore has an established market price at lower Lake ports. For State taxation purposes, all accounts reflect the value of the ores f.o.b. cars at mine or property. *Therefore, it is logical to peg "gross income from the property" f.o.b. cars at mine. The same basis is logical and practical in all other iron mines throughout the country.* [Italics supplied.]

Finally, it should be stated that this subject has had careful consideration for several months. Its details and difficulties have been thoroughly discussed with the taxpayers in the various industries and the bases established are thoroughly understood. All nonferrous metal sales are based on or reflect the established New York quotations.

While the final drafting and proper phraseology of the definitions in the regulations must be made by those legally appointed and qualified for the work, the *following tentative suggestion is proposed* by the engineering section of the bureau, in order to cover the details involved. [Italics supplied.]

For the purpose of this subdivision "the gross income from the property" shall be the competitive market receipts, or its equivalent, received from the sale of the crude, partially beneficiated or refined gold, silver, or copper, *the product actually disposed of by the taxpayers to govern the method of computation of receipts in all cases, and in the case of all other metals, coal and oil and gas, the competitive market receipts, or its equivalent, received from the sale of the crude products, or concentrates on an f.o.b. mine, mill, or well basis.* [Italics supplied.]

The "net income of the taxpayer (computed without allowance for depletion) from the property" shall be determined by deducting all allowable expenses except depletion from "the gross income from the property" as defined above. In the case of leases the "lessor's income shall constitute the royalties and the lessee-operator's income shall constitute the gross receipts less the royalties."

## Joint Committee Hearings, 1930

(Depletion of Mines, Hearings before the Joint Committee on Internal Revenue Taxation, 71st Cong., 3d Sess.)

- [2] Statement of L. C. GRATON, Cambridge, Mass., on behalf of various interested parties:

Mr. GRATON. My name is L. C. Graton. I reside at Cambridge, Mass. I am a mining geologist by profession.

The CHAIRMAN. Without objection, the witnesses will be allowed to complete their statements in a connected order and then members of the committee will ask questions at the conclusion of the statements. Whom do you represent, Mr. Graton?

Mr. GRATON. I speak for a group of taxpayers from various parts of the country and for one taxpayer, a domestic corporation, who operates outside of the country, the Cerro de Pasco Copper Corporation.

The CHAIRMAN. Proceed with your statement.

Mr. GRATON. What I have to say Mr. Chairman and members of the joint committee, is entitled "Preliminary Outline of Testimony."

[5] SYNOPSIS OF TESTIMONY

The first approach to our subject is through an analysis of the inherent nature of mine value, the peculiar characteristics of property in mineral deposits conferred upon them by the geological conditions of their occurrence and recognized by man on account of their inherent validity. \* \* \* In short, the whole of his possession in mineral consists of capital, and the measure or value of that capital is the value of the whole of the mineral.

[6] The oft-stated assertion that the mine owner's right to depletion as a deduction from taxable income rests upon statutory grant and not upon constitutional right is shown to be contradicted within the revenue laws and regulations themselves, by common sense, by general law, and by highest tribunal.

Analysis of the successive revenue laws indicates that they have not proceeded as from a firm basis of theory, principle, and practice relating to mine value and the nature of depletion, but that instead the laws represent a groping for and toward the truth, with, happily, some substantial progress attained in that direction.

But the degree of progress is as yet insufficient to meet a fair test as to satisfactory character. In consequence of deficiency in the law—or which at least the clumsy wording of the law permits to enter in its administration—the mining industry has suffered, and still in substantial measure suffers hardship, discrimination, and unnecessary expense, as well as uncertainty and embarrassment in its proper undertakings.

Relief is imperative and may only be hoped for through such change in the law as will clearly specify the relief required. Fortunately, however, there exists a means whereby modification of the law may be made in the simplest possible manner, namely, by the amendment of a single paragraph in the present law in such a way as to substitute for the existing paragraph a new one which relates to depletion for mines, and which closely accords in form, substance, and spirit with the immediately succeeding paragraph already enacted regarding depletion for oil and gas wells.

The new paragraph proposed as a substitute is as follows:



(2) *Percentage depletion for mines.*—In the case of mines the allowance for depletion shall be  $33\frac{1}{3}$  per centum of the taxpayer's net income as defined in section 21 (computed (a) without allowance for depletion, and (b) excluding such items of gross income and deductions as are not directly attributable to the operations of mineral or metal production from the property), except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.

*This simple solution of a long-standing vexatious difficulty is made possible through utilization of the percentage method for determining depletion, a method simple in its conception and application, but indeed almost magical in its effects. For its adoption would thenceforth avoid all necessity whatsoever for the troublesome matter of mine valuation, would enormously simplify administration, and would, in our belief, remove virtually all of the iniquities and hardships which various portions of the mining industry now suffer, whether judged by standards within the industry itself or as against taxpayers in other groups. [Italics supplied.]*

[7]

While the earliest grist of mine valuations was in progress, the bureau became advised of an alternative method of determining a reasonable and proper deduction for depletion, which determination was in most instances the object of valuation. This alternative method was the percentage method, to which allusion has already been made, and it is important to note that earnest recommendations that the bureau forthwith adopt this method were made independently by bureau engineers who came most intimately into con-



tact with the operations and limitations of the analytic appraisal method.

The method of determining depletion as a fixed percentage of net income, before the deduction of depletion, is then clearly discussed, and its derivation demonstrated. It is shown to test in essence on a reduction to present worth of the operating earnings of the property in just the same way that the analytic appraisal method aims to do, and it yields the same kind of separation of these operating profits into return of capital and true profit that the other method does. In fact, the percentage method may be described as the purified essence of the analytic appraisal method whereby all the crudities and uncertainties, all the assumptions and the differences of judgment are mainly, if not entirely, eliminated, and the true answer, or a close approximation to it, automatically furnished in every instance. It affords, year by year from the beginning, the true yearly quantities, of depletion which the mine owner would receive if he were able to know at the outset the exact content, nature and grade of all the profitable mineral embraced within his boundary lines, which constitutes his capital. It makes the determination for each year subject to the facts applicable to that particular year. Like a spring balance, it weighs whatever is placed in its scale pan and automatically returns the correct answer. It is always right, it is never wrong. It is the essence of fairness and justice.

The percentage method of determining depletion has been in sole use for this purpose by the department of national revenue in the Dominion of Canada since the taxable year 1915. And as evidence which we shall present clearly shows, it has been found to give well-nigh universal satisfaction to all concerned

and is enthusiastically supported by taxpayers and government.

[8] Among the objections that have been raised to adoption of the percentage method in our Federal laws is the assertion that serious administrative difficulties would attend the effort to derive the net income from the property in order that ~~this~~ might be used before deducting for depletion as the base against which the percentage should be applied, to derive the proper depletion allowance. In reply to this objection we present expert testimony to the effect that the bureau has been required for years to determine the net income for mineral property in connection with other provisions of the law and that there is no indication as yet on record to show that such determination has been so difficult as to lead to serious controversy. On the contrary, experience with the accounts of great and complicated mining corporations, as well as those of more modest dimensions and scope, clearly indicates that there will be no difficulty in determining the net income for purposes of depletion deduction. As provided in the proposed amendment, the net income to be used is that which *should* be used namely, the net income as specified in the act itself, and the use of this net income, which must in any event appear in the tax return of every company, will still further simplify the determination of percentage depletion in the way we recommend. [Italics supplied.]

[9]

\* \* \* We feel, therefore, that your committee has performed a distinct public service in having assembled and published *the preliminary reports on de-*

pletion by your investigating staff, under the leadership of Mr. L. H. Parker. Members of the mining industry appreciate and welcome this highly important information otherwise inaccessible to them. [Italics supplied.]

With the major conclusions of that report on depletion for mines, the group for whom I speak is in general and substantial accord and we find the chief recommendations of that report impressive indeed. [Italics supplied.]

\* \* \*

[12] Mr. GRATON. \* \* \*

The situation is this: To our best belief and knowledge, all members of the mining industry, as distinguished from the gas and oil industry, now believe, if they have not always believed, *that net income for mines is a preferable basis for the use of a percentage method than gross income*, which is adopted in the case of oil and gas companies as the basis against which a fixed percentage is to apply. We think that net income is a far fairer expression of ability to pay, of the measure of the capital that is sacrificed or parted with when the mine owner sells his property. [Italics supplied.]

Mr. COLLIER. Let me ask you one question there, please. Why?

Mr. GRATON. Because value is derived directly through profit. If there is no profit, there is no value, and value is the capitalization of the present worth of the profits to be enjoyed. Net income is the expression of those true profits and, therefore, depletion which is a compensation for the value, the part of the value parted with, within the limits of any taxable year is and must be related in a very definite way to the profits of which it is an expression. The net income, therefore, before depletion deduction shall

have been subtracted from it, is the basis for application of the depletion percentage. Our proposed amendment suggests that  $33\frac{1}{3}$  per cent of that net income be determined as the appropriate amount.

Mr. COLLIER. Well you are representing the mining industry, and you are now laying down a principle; you think the law as written in reference to the gas and oil industry should be changed from gross also to net income? You are laying down a principle, I believe, now?

Mr. GRATON. Sir, I think it would be preferable—I think it would avoid the possibility of our getting beyond our depth—if we experts, as we believe, in the mining industry seek to confine our presentation to the industry which we know. I do not wish to evade your question, sir.

[14]

Statement of AXEL P. RAMSTEDT, Wallace, Idaho:

Mr. RAMSTEDT. The subject of my remarks is The Nature of Mine Value and of Depletion Unique Character of Mine Value.

[17]

#### THE NATURE OF DEPLETION

Depletion means literally an emptying or subtracting. In its broad economic significance as applied to mines, it is the loss which the mine owner suffers, or the reduction of his property and capital which he experiences, through the production and sale of mineral. In a somewhat more special and derived sense depletion is used to mean compensation for the loss or reduction so suffered. It is in this last sense of compensation for diminution of property or capital that depletion is used in the revenue laws. The normal

and necessary function of a mine is to produce mineral for sale at a profit, and such production and sale gradually and progressively exhaust the property, [18] because the total quantity of profit-yielding mineral in the property is finite and limited in amount. Depletion is, therefore, experienced for each unit of profitable mineral removed from the property by mine operation.

When we come to inquire how much depletion in the sense of compensation for loss a mine owner must provide for, we find that there is only one true answer. He must provide depletion for all that he removes from the property. Hand in hand with progressive exhaustion must go compensation for such exhaustion. If his productive operation eventually exhausts the entire profitable mineral content of the property, then his progressively accumulated depletion must have been such as to compensate him for such entire exhaustion.

\* \* \* \* \*

[27]

\* \* \* \* \*

Having considered the question of depletion determination as a fixed percentage of net income before depletion at several of its previous meetings, the American Mining Congress at its annual meeting in Washington in December, 1929, adopted unanimously a resolution favoring the incorporation into the law of such a method of depletion determination. In conformity with that expression of view, and after conference with responsible members of the Revenue Bureau, and specifically in response to written request by the honorable chairman of the Joint Committee on Internal Revenue Taxation, I submitted to your committee a proposed amendment to the exist-



ing revenue law which specifically approves the determination of depletion by the percentage method as based on net income before depletion allowance has been deducted. That amendment is as follows:

That section 114(b) of the revenue act of 1928 be amended by substituting for subdivision (2) of said section 114(b), the following:

"(2) *Percentage depletion for mines.*—In the case of mines the allowance for depletion shall be  $33\frac{1}{3}$  per centum of the taxpayer's net income as defined in section 21 (computed (a) without allowance for depletion, and (b) excluding such items of gross income and deductions as are not directly attributable to the operations of mineral or metal production from the property), except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph."

*While it appears now to be the unanimous feeling of all those who have expressed themselves upon the subject that net income before depletion deduction rather than gross income should be the proper basis for determination of depletion for mines by a percentage method, the foregoing proposed amendment has in all other respects carefully followed, so far as appropriate, the form, substance, and spirit of the succeeding subdivision 3 of section 114(b) of the 1928 act relating to percentage depletion for oil and gas wells, a provision which has been operative since 1926. [Italics supplied.]*

The foregoing proposed amendment for mines means that the allowance for mines shall be  $33\frac{1}{3}$  per cent of the taxpayer's net income before deduction for depletion, carried through to the end of the taxpayer's operation of mineral or metal production, provided that the allowance shall not be less than it

would be if computed on the basis of cost or of value as of March 1, 1913. [Italics supplied.]

[29]

Statement of WILLIAM J. FRIEDMAN, of Chicago, Ill., representing the Building Stone Association of Indiana, the Indiana Limestone Co., and the Ingalls Stone Co.:

Mr. FRIEDMAN. Mr. Chairman and gentlemen of the committee, my name is William J. Friedman. I am an attorney of 310 South Michigan Avenue, Chicago, Ill. I appear in behalf of the Building Stone Association of Indiana, the Indiana Limestone Co., and the Ingalls Stone Co.

[30]

I am presenting this case on behalf of the Building Stone Association of Indiana, the membership of which consists of 16 representative companies, the Indiana Limestone Co. and the Ingalls Stone Co. The production of these organizations is 98 per cent of the aggregate amount of Indiana limestone produced. In other words, I am representing practically the entire Indiana limestone industry at this hearing. \* \* \*

[33] Four methods of revising the present system of depletion are suggested in the preliminary report on depletion submitted to your committee. The operators of Indiana limestone quarries feel that they are entitled to immediate relief from the oppressive administration and operation of the present law. They

will welcome any plan which helps them to obtain the relief to which they are justly entitled.

They have examined the four methods presented (or three, if the two methods of percentage of net income are considered as a unit), and feel that a fixed rate of depletion per cubic foot of stone would probably be most satisfactory. This conclusion is based upon the fact that such a method would probably be the simplest. But in view of the fact that such a basis of depletion may not satisfy the requirements of other mining interests and fulfill the requirements of the Treasury Department as satisfactorily as any of the other methods proposed, the operators of Indiana limestone quarries are willing to accept any plan acceptable to the other mining interests [p. 34] and the Treasury Department which will give them a fair and equitable basis of depletion.

[36]

Statement of J. F. CALLBREATH, Washington, D.C., secretary of the American Mining Congress:

Mr. CALLBREATH. My name is J. F. Callbreath. I am secretary of the American Mining Congress, Munsey Building, Washington, D.C.

Mr. Chairman and gentlemen of the committee, our annual tax conference met in Washington last week. We were favored with an address by the chairman of this committee, and other addresses followed. The conference was unable to agree upon a definite and complete statement to be presented to this committee; but they did agree upon a resolution which I beg to present to you:

*Resolved*, That it is the judgment of this meeting, representing a large majority of the mining industry, that present United States

revenue laws governing depletion of mines should not be disturbed, except that some amendment to the provisions relative to discovery should be made so as to avoid, as far as possible, discriminations regarding which complaints are now made; and that a committee be appointed by the chairman to prepare such amendment and to take such action as it may deem advisable to further it; and be it further

*Resolved*, That if provision for percentage depletion is adopted, it should be at a rate of not less than  $33\frac{1}{3}$  per cent of net income before depletion, and should in no event be less than depletion under existing law.

[44]

Statement of JAMES C. DICK, Salt Lake City, Utah:

THE ANALYTICAL APPRAISAL METHOD OF MINE VALUATION AND THE UNIT METHOD FOR DETERMINING DEPLETION

[47]

I believe one becomes more convinced with the accuracy, justice and equity of the percentage of income method for determining a reasonable depletion the more he studies the question. \* \* \*

[48] *All that the percentage of income for depletion deduction means is that, were we to make an appraisal by the present value method, the factors we would use in the determination of depletion by the unit method have been automatically corrected, and the annual allowance by the percentage method will be close to the true figure, rather than an erroneous de-*

duction that may result from the use of factors based upon assumption or conjecture. We are not estimating the quantity of ore, nor the grade, nor the selling price of metal, nor the metallurgical difficulties that we may have, nor the conditions over which we have no control, but we are basing the deduction on past experience, confirmed by the exhaustive report of the staff of the congressional committee, that  $33\frac{1}{3}$  per cent is about the proper average deduction from income to compensate for the wasting of the taxpayer's capital in his operation. [Italics supplied.]

[49]

#### CONCLUSION

From my experience in the Bureau of Internal Revenue, employed as valuation engineer, and as head of the natural resources subdivision, and from experience in the practice of my profession as a mining engineer, I am of the opinion that  $33\frac{1}{3}$  per cent of the net operating income is a reasonable depletion allowance. I do not believe in a deduction based upon the gross income, as gross income means but little in the operation of a mine. I am fully convinced, however, that a depletion deduction based upon the net income is the true procedure. That to arrive at a reasonable depletion allowance of a property, not fully developed, by determining the value of the unit of metal mined each year by an analytical appraisal, such as is now the present practice of the bureau, does not approach the accuracy which would result by deducting  $33\frac{1}{3}$  per cent of the income.

[50]



Mr. COLLIER. While I know in this further question I am directing it to one who is not speaking either for the gas and oil industry or qualified as an expert, could you give me any reason why this system, which would be so beneficial to the mining industry, would not also be beneficial to the gas and oil industry?

Mr. DICK. No. I understand, sir, on the contrary, it has been found to be beneficial or satisfactory, to the oil industry. *Of course the depletion deductions of an oil producer are not the same as the depletion deduction of a mine operator. One reason is that oil has a value pretty much as it comes out of the ground. The miner must take his ore, in the majority of cases treat it, operating by concentration or by direct treatment at the smelter.* [Italics supplied.]

[56]

Statement of F. G. HAMRICK, New York, N.Y.:

#### DETERMINATION OF NET INCOME

[57] It would appear that the determination of net income from the property in connection with discovery depletion has given rise to no serious administrative difficulty. I say this because I have been unable to find any record in the decisions of the Board of Tax Appeals or the courts to indicate that the amount of net income for the purpose of determining depletion based on discovery has been a matter of litigation.

It must be obvious that if administrative difficulties are absent in determining net income from the property for the purpose of applying the limitation in case of depletion based on discovery, they will also be lacking in determining net income from the prop-

erty for the purpose of measuring the depletion allowance.

Even if there did not exist the well established precedent for the determination of net income in connection with discovery depletion, the necessity for determining net income under the proposed percentage depletion plan would not entail either insurmountable complications or even new procedures in administration. The net income before depletion of the company whose activities are confined to mining is reported of necessity in its income tax returns.

\* \* \* Where the taxpayer's interests are varied, as in cases of large mining companies, there is, I believe, no doubt that as a rule its books reflect the result of each operation, which makes it possible for the taxpayer to determine to the satisfaction of the Bureau of Internal Revenue *the portion of the income applicable to mining*. Efficient management and good accounting demand that the books of the taxpayer be kept in sufficient detail to furnish such information. [Italics supplied.]

In addition to the assurance our own experience furnishes, we know that the Dominion of Canada has for many years not only determined the net income from mining properties, but has actually applied the net income so determined, as a measure for the depletion allowance by the percentage method. For the purpose of determining the taxable income in the Dominion of Canada, allowable depletion in the case of nickel, copper, lead, zinc, tin, and asbestos properties is  $33\frac{1}{3}$  per cent of the net income from the property.

[58] For the reasons given herein, it seems certain that the determination of "net income" from mining properties can be computed, and in fact is now being computed, by both the taxpayer and the Bureau of

Internal Revenue. Furthermore, it is evident that the substitution of percentage depletion for discovery depletion would not create any complication whatsoever in the determination of net income. On the contrary, the substitution of percentage depletion for discovery depletion would yield a simpler determination of the depletion allowance than that now required in connection with discovery depletion, since there would be no necessity for valuations, and it would effectively promote the highly desirable end of prompt determination by the taxpayer of the magnitude of his tax obligation.

[63] Statement of JAMES F. MCCARTHY, of Wallace, Idaho, president and manager of the Hecla Mining Co.:

\* \* \* \* \*

#### A MINE EXECUTIVE'S COMPARISON OF UNIT DEPLETION AND PERCENTAGE DEPLETION

Mr. MCCARTHY. My name is James F. McCarthy. I am president and manager of the Hecla Mining Co., Wallace, Idaho.

I am submitting herewith a statement concerning depletion as applied to mines, and a plea for the favorable consideration by your committee of the proposal before you to substitute percentage depletion on net income for the present discovery provision.

Viewing this proposal from the position of the executive or business manager of a mining operation, there appear the following respective advantages and disadvantages:

Advantages in percentage depletion:

- \* \* \* \* \*
1. Simplicity of the proposed method as contrasted with the present complex method.
- \* \* \* \* \*

2. Accurate and easily determined basis under percentage depletion contrasted with the lack of accuracy under the present method.

[89]

Statement of Hon. DONALD A. CALLAHAN, of Wallace, Idaho, president of the Callahan Zinc-Lead Co.:

#### AN OPERATOR'S EXPERIENCE WITH DEPLETION

[94]

Under the present laws we find that capital is often taxed under the guise of income, and as a result not infrequently one miner is compelled to pay twice the taxes of his neighbor who to all intents and purposes is similarly circumstanced. The properties are alike as two mines may be, costs are identical, the product is sold in the same market at the same price, and operating earnings are equal; yet, through the workings of the system for computing the depletion deduction, one pays twice the taxes of the other. Through the presence or absence of fortuitous circumstances over which the owners have no control, one man receives no recognition whatever of capital value and has no depletion and pays tax on both capital and income, while the other, under the discovery clause, is allowed, and properly so, the return of his capital values free of tax. \* \* \*

[95]

We are willing to accept that suggestion and *that is why we are before this committee presenting a simple, practical, workable plan for doing away with the gross discrimination and injustice unavoidable*

*under the present law.* In this endeavor we ask the cooperation and assistance of the bureau and the Treasury Department. \* \* \* [Italics supplied.]

[104] Statement of B. H. BARTHOLOW, Special Assistant to the Secretary of the Treasury:

Mr. BARTHOLOW. B. H. Bartholow, Treasury Department, Washington, D.C.; special assistant to the Secretary of the Treasury.

\* \* \*

[110] \* \* \* Therefore the allowance of percentage depletion in the mining industry would effect a vast change because it would grant to all instead [p. 111] of relatively few the special tax benefit or exemption, which Congress has heretofore accorded only to those who risked their capital and made discoveries of new ore bodies. Furthermore, while the bureau is having difficulty in administering the percentage depletion provisions in the case of oil and gas wells, the Treasury believes that the problem of administering like provisions in the case of mines would be infinitely greater. The foremost reason is that the field price of the oil or gas at the well indicates the income from the property, while in the mining industry, where there is no general field price for the ore at the mine and where the larger taxpayers do their own concentrating, smelting, refining, transporting, and marketing, all that is known is that the refined or fabricated product was sold for a certain amount. *There is thus presented the insuperable difficulty of dividing up the resulting income among all those various activities—marketing, transporting, smelting, refining, mining, etc.—and then allocating the proper portion to the mining operation which would be the income from the mine.* [Italics supplied.]

[114]



Mr. COLLIER. There is one thing I want to ask you in regard to the change of the law in 1926, in which we first went to the percentage basis on gas and oil wells and gave them 27½ percent depletion on gross income: How is that working out? Is that satisfactory both to the Government and the taxpayers now; has it proved a success?

Mr. BARTHOLOW. My information relates to its administration. Numerous complicated, technical issues having to do with the determination of the net income even from oil properties, where there is a field price, have arisen, and there are still unsettled technical problems of all kinds. I could enumerate a few here, but they are quite detailed. This much is certain, those who are administering the law find the percentage depletion provisions more difficult to administer than the provisions for basic depletion.

[116]

Further statement of L. C. GRATON.

[127]

We have been greatly interested in the preliminary report on depletion. We commend Mr. Parker for the work that he has put on it and for the conclusions that he has drawn, and the committee for its vision in having such information made available. Although we can not fairly say that we agree with all the details included in that report, as perhaps is not to be expected, we do feel that it is an earnest, constructive, contribution and, with its fundamental considerations, we find ourselves in absolute accord.

We have no fear of meeting, with absolute conclusiveness, the presentation made by the Treasury De-

partment this morning. \* \* \* [128] As to the question of revenue, it was indicated that the facts were not sufficient to make a final conclusion, but the estimates were that, for the metal-mining industry, the whole of the metal-mining industry, if discovery depletion were displaced by percentage depletion, the loss to the Government might be estimated at \$200,000 for that year, with an indication that such loss would gradually decline. And that \$200,000, it was said, along with similar estimates for some of the other industries, was a very conservative estimate, so far as the Treasury is concerned, and the chances were that the true loss would be less than the estimate.

Now that appears as the most approximate, the most definite estimate of the effect on revenue of the percentage depletion scheme that I have learned and, as far as I can see, if that applied, as I imagine it did, to the tax year of 1926, *it would mean a reduction of revenue of one and a half per cent of the taxes paid by the whole of the metal mining industry.* [Italics supplied.]

\* \* \* \* \*

1932

[Percentage depletion was extended to coal, sulphur and metal mines in the Revenue Act of 1932, c. 209, 47 Stat. 169. The Ways and Means Committee made no recommendation in that connection. Sulphur was added on the House floor at 27½ percent. The Senate Finance Committee reduced this to 23 percent and added metal mines at 15 percent (S. Rep. No. 665, *infra*, pp. 130-131). Coal, at 5 percent, was added on the Senate floor (75 Cong. Record 10418-10419) and the House conferees accepted the Senate amendments (H. Conference Rep. No. 1492, *infra*, pp. 131-132). Material excerpts from the hearings, and reports fol-

low, together with the statute and the Treasury Regulations which were subsequently promulgated in implementation of the statute.]

House Hearings, 1932

(Revenue Revision, 1932, Hearings before the Committee on Ways and Means, House of Representatives, 72d Cong., 1st Sess.)

[327] BASIS FOR DEPLETION ALLOWANCE

Statement of BERT E. HANEY, Portland, Oreg., representing the Northwest Mining Association:

Mr. HANEY. Mr. Chairman and gentlemen, I represent the Northwest Mining Association, and I want to make a few remarks with respect to the subject of depletion of mines. It is unnecessary to do more than this, because this matter was very fully presented to the joint committee on internal-revenue taxation at hearings held December 9, 10, 11, and 12, 1930. Those hearings were published and are of course available to members of this committee. Moreover, there are four members of this committee who were also members of the joint committee on internal-revenue taxation when those hearings were held.

Our cause for complaint at these hearings rested primarily upon the following contentions: *First, that depletion allowances in the case of mines are inequitable as between taxpayers in the same industry; second, that the depletion allowances were uncertain and were subject to excessive controversy; third, that the determination of the depletion allowance was expensive both to the Government and to [328] the taxpayer, and we still rest our appeal for relief on those three contentions. [Italics supplied.]*

When I say relief, I do not wish the members of this committee to infer that in these times I am asking

for anything which will decrease the total taxes paid to the Government by the mining industry. What we are asking is that the total of the allowances now made be spread *in an equitable manner over all taxpayers in the industry*, so that all may compete on an equal basis. [Italics supplied.]

Under the present system some properties are receiving no depletion allowance, while competing properties are practically exempt from taxation by virtue of such allowances.

It may well be asked, can this be done? My answer is plainly, yes. Congress itself has answered this question by abolishing the depletion system for oil and gas wells as early as 1926, and adopting a system based on a fixed percentage of income. Moreover, Canada has long used the percentage-depletion system for all of its mines and its oil properties with marked success. The identical system which was abolished for oil and gas wells in 1926 is the same inequitable system which remains in the law to-day with respect to mines.

The group which I represent *urges that the inequities of the mining industry with respect to depletion be eliminated* as they were in the case of oil and gas wells by applying the percentage system. *In our case we would have no complaint if the percentage should be applied to net rather than to gross income*, although the net income basis is less favorable to the taxpayer. However, since the technical staff of the joint committee on internal-revenue taxation, in its exhaustive report published on this subject, suggests the net basis as being more certain to render a fair revenue to this Government, it appears proper that there should be no controversy raised on this particular phase of the subject. In fact, at the hearings before the joint committee my group asked for depletion based on a percentage of net income. In the hearings before the

joint committee facts were shown that indicated a depreciation allowance of  $33\frac{1}{3}$  percent on the net income would be fair allowance and not result in decreased taxes. This appears to have been the conclusion urged in the report of the staff of the joint committee. However, our particular group will not attempt to dictate to the committee what that percentage should be. We will be content to rest entirely upon the fairness with which you have treated past problems and with which we think you will undoubtedly treat this problem. [Italics supplied.]

The *inequities in the present system* came about very largely because of the difficulty in valuing mines. \* \* \* [Italics supplied.]

[329] Just one more word before I close. At the present time the Government should make a substantial gain in revenue by adopting the percentage depletion system. Profits now are low and in many cases the depletion allowance completely eliminates the net income, so there is no tax. Under the percentage plan, if there is no operating profit before the depletion deduction is taken, then at least  $66\frac{2}{3}$  percent of that income will be subject to a tax, and any measure which will equalize the revenue between the years of high and low profit should appeal to this committee now that we are faced with a deficit which is somewhat attributable, at least in part, to a sudden decrease in the income tax collections.

In conclusion, Mr. Chairman, I want to appeal to the committee to correct the *present inequitable depletion system* in the present bill. It is vital to many of our taxpayers, if they are to be permitted to exist at all in the mining business. We can not compete under heavy taxes with those similarly situated mining the same kind of ore at the same cost, who are



paying no taxes. \* \* \* [Italics supplied.]  
[330]

The CHAIRMAN. When the American Mining Congress were opposing this, I understood you to say it was a divided question with them, that they were not, as an organization, opposing it. Am I right in that?

Mr. HANEY. May I state my understanding of it, Mr. Chairman? My understanding of the matter is that the Mining Congress has not in recent years taken a position for or against percentage depletion, that there is a division concerning that subject within the membership. The Mining Congress is made up of gold miners, silver miners, lead miners, tin miners, coal miners and many other kinds of miners. Some of the groups take our position, some of the groups in the Mining Congress, noticeably the gas and oil people, are not enthusiastic about this plan. They already have it. They have what we are asking for.

[331] Mr. LEWIS. Mr. Chairman, if no others wish to ask questions, I would like to ask quite a few.

Mr. CHINDBLOM. Then, let me ask one, if I may. The basis for depreciation and depletion set forth in section 114 gives special rules only *as to mines, or minerals being the product of mines*, and oil and gas, being the product of wells, producing those articles. Are there any other classes of property, or classes of production, to which similar or special rules might be applied in justice or equity to these three classes? [Italics supplied.]

Mr. HANEY. I do not know whether I understand you, but I will try to answer you, sir. To start with, I understand that with respect to gas and oil the depletion is computed on a percentage basis under the present act, that with respect to ore mines, it is com-

puted on this so-called analytical method. Depletion in a mine is not—and you will bear with me when I say I am not a miner, sir, and I am discussing a rather technical subject—depletion in a mine is not exactly the same thing as depreciation in other personal property, but it is somewhat akin to it. Depletion in mining is a method of determining what is capital and what is profit. \* \* \* The trouble is that our present system is so purely a matter of guess that it has resulted in glaring inequalities, inequalities where two men in the same community, operating the same kind of a mine, at the same price, and producing the same ore, one of them is paying an enormous tax and one paying no tax, both of them honest, one of them a good guesser, and one not.

[335] Mr. LEWIS. What is your suggestion?

Mr. HANEY. *I say this method is just another method of computing that depletion, and it is the same method and will provide the same result as the present method would produce if there were no mistake ever made in the present method.* [Italics supplied.]

[336] Mr. CHINDBLOM. I was going to ask whether Mr. Parker and others who are always available to us will not discuss this matter when the committee takes it up?

[337] The CHAIRMAN. Mr. Chindblom, I think our understanding is when we meet to go into consideration of the drafting of the bill, *we expect to have Mr. Parker and other experts with us to take up all these propositions and discuss it with them before the committee reaches any conclusion.* [Italics supplied.]

Statement of E. T. CUMMINS, Washington, D.C.,  
representing Domestic Sulphur Producers.

Mr. CUMMINS. Mr. Knoblock has asked me to represent him and present certain matters to this committee in which we are jointly interested.

Mr. CRISP. You represent whom?

Mr. CUMMINS. I represent one of the sulphur companies interested in the matter, the Freeport Sulphur Co.

The Freeport Sulphur Co., the Texas Gulf Sulphur Co., and the Duval-Texas Co. ask you to make a slight amendment to section 114(b)(3) of the 1928 revenue act, which deals with depletion of mines, or particularly the oil and gas section of that provision.

We are not here asking for any relief from the paying of taxes, but only that certain matters involving valuation and resulting depletion be clarified or simplified. *In other words, we are asking to be put in the same class as that of the oil and gas industry regarding depletion.* Our particular reasons for this request is that the production of sulphur is very similar to that of oil and gas. More so than the ordinary mining operations that are carried on by the mining industry. That [338] is, we drill holes for its production, pump it out of the ground and recover by that method. [Italics supplied.]

Our relations are always with the oil people, inasmuch as they usually operate on the same dome, or along with us, or own an interest in the property from which we obtain production.

The section we ask to be amended now reads:

Percentage depletion; in the case of oil and gas wells, the allowance for depletion shall be 27.5 percent of the gross income from the property.

All that we are asking you to do is to insert the word "sulphur" so that section will read "in the case of sulphur, oil and gas wells," and we believe and are sure that the insertion of this provision into the law will clarify it and make it more simple in its operation. It will let us know where we stand with regard to our taxes each year as they are due. It is not going to reduce our taxes and it will be cheaper in its operation, that is, so far as the Government is concerned, and cheaper for us.

I shall be glad to answer any questions relative to this proposal that you gentlemen may care to ask. I would also like to present our brief on the subject and ask permission to have it printed in the record.

Mr. CRISP. You have that permission, and on behalf of the committee we thank you for your presence.

(The brief is as follows:)

#### BRIEF ON BEHALF OF SULPHUR PRODUCERS

CHAIRMAN WAYS AND MEANS COMMITTEE,  
*House of Representatives of the United States.*

DEAR SIR: The following brief is submitted on behalf of the Freeport Sulphur Co., Texas Gulf Sulphur Co., and Duval-Texas Sulphur Co., being all of the producers in the United States of sulphur by the Frasch process; that is, recovery through driven wells. They represent in excess of 99 percent of the total production of sulphur in the United States. (See Mineral Industry, 1930, p. 560.)

These producers unite in requesting an amendment to section 114(b)(3) of the revenue act of 1928 so as to include sulphur in the percentage depletion granted to oil and gas wells.

\* \* \* \* \*

[339] I. THE MINING AND PRODUCTION OF SULPHUR BY THE FRASCH PROCESS. BY USING DRILLED WELLS RENDERS THIS MINING OPERATION MORE SIMILAR AND ANALOGOUS TO OIL AND GAS WELLS THAN TO METAL MINING

The Frasch process of mining sulphur (under which over 99 per cent of the production in the United States is obtained) is:

First, to sink a well into the caprock which overlies the core salt core of the salt dome in which these deposits of sulphur occur. These wells are drilled with a rotary rig similar to that employed in the petroleum industry for work in soft formations. Second, into this same well is pumped water heated under pressure to a temperature above the melting point of sulphur. This melts the sulphur in situ. Third, it is then pumped to the surface by compressed air. The sulphur arrives at the surface in a liquid form. Fourth, it is then distributed into bins where it is allowed to solidify, for immediate sale and distribution. *The sulphur so recovered is in excess of 99.5 per cent pure and is of the grade used in commerce. It requires no further treatment or refining to prepare it for the trade. [Italics supplied.]*

II. SIMILAR TO OIL AND GAS SULPHUR IS A COMMERCIAL PRODUCT AT THE MINE AND DOES NOT HAVE TO BE SUBJECTED TO A FURTHER TREATMENT FOR SALE

*Sulphur, like oil and gas, has a value as it comes out of the ground. Similar to oil and gas there is an established field price for sulphur which indicates directly [p. 340] the income from the property. In the case of ores of the metals there is no general field price for the ore at the mine and when the taxpayer does its own concentrating, smelting, refining, trans-*



porting and marketing, all that is known is the selling price of the refined or final product. *Contrasted with this situation of the ores of the metals sulphur, oil, and gas have a field price and no profit derived from the process of their further treatment could be the subject of depletion.* [Italics supplied.]

Percentage depletion, therefore, is peculiarly appropriate for sulphur, together with oil and gas wells, and avoids the difficulty existing in the case of metal mines of allocating the proper portion of the income between that which was due to the mining operations simpliciter and that which was due to smelting, refining, transporting, etc.

\* \* \* \* \*

[341] VI. NUMEROUS TAX QUESTIONS ARISING OUT  
OF THE DISTRIBUTION OF DEPLETION DIVI-  
DENDS WILL BE AVOIDED

\* \* \* \* \*

We need not dwell upon the various other general arguments in favor of the percentage method, such as its simplicity, accuracy and ease of determination, economy of administration, prompt settlement and equality, which have already been stressed by others before this committee.

We base this application upon the close association of ownership and discovery between sulphur and the oil and gas wells, the multiple nature of the various interests in the sulphur domes and the unique method of producing and mining sulphur, essentially similar to that of producing oil and gas, and the fact that *there is for sulphur, as for oil and gas, a field price that avoids any allocation in determining the income to which percentage depletion is applicable.* [Italics supplied.]

## SUMMARY OF ADVANTAGES

The advantages may be briefly summarized as follows:

1. The production of sulphur in the United States is analogous to the production of oil and gas.
2. It would eliminate the complex question of valuation for depletion purposes.
3. It would be simpler in its administration.
4. It would be accurate and easily determined.
5. It would allow prompt settlement.
6. It would produce equality in the result.

All of which facts we submit warrant the classification of sulphur producers of this country for depletion with the oil and gas industry.

Respectfully submitted

H. F. J. KNOBLOCH.

E. T. CUMMINS.

[342] BRIEF OF THE NATIONAL COAL ASSOCIATION AND  
SUNDRY DISTRICT ASSOCIATIONS OF BITUMINOUS  
MINE OPERATORS

WASHINGTON, D.C., *January 23, 1932.*

TO THE WAYS AND MEANS COMMITTEE,

*House of Representatives, Washington, D.C.*

GENTLEMEN: The signers of this brief urge your earnest consideration of the following statement regarding the need of the coal mining industry for relief through appropriate modification of the present depletion provisions of the internal revenue act. The brief is submitted on behalf of bituminous mine operators with the indorsement of their national organization, the National Coal Association, and of the local and district associations in the industry whose signatures are appended below.

We feel that we are justified in demanding such relief on the general ground that however uniform and equitable the present depletion provisions may sound, in practice they have been applied in such a way as to amount to a serious discrimination against the coal mining industry as compared with other mining industries.

It is a well-recognized principle of taxation that no system can be regarded as equitable under which the burden of taxation rests unequally upon different taxpayers of the same class. As will be demonstrated herein, the coal mining industry for many years has been taxed to an inequitable extent in comparison with other mining industries. \* \* \*

The inequitableness of the tax burden laid upon the coal mining industry arises chiefly from the practical effect of the present provisions of the internal revenue act relating to the depletion of mining properties. \* \* \*

Apart from the petroleum industry all mining industries seem to be treated alike in the matter of depletion so far as the wording of the statute is concerned. In the practical application of the law, however, great inequalities have arisen. These have resulted chiefly from two causes.

In the first place, the coal mining industry in 1913 was in a very depressed condition. Consequently the values established for coal lands at that time were inadequate. There were few sales of mining properties, and those that took place were made under circumstances tending to reduce rather than maintain established values. For lack of current earnings few companies were able by the use of the analytical appraisal method to provide adequate value for their mining properties. \* \* \*

In the second place, the coal-mining industry has derived no benefit from the discovery-value provision of the act, while other branches of the mining industry have been able to set up current values for substantial percentages of their output through their ability to take advantage of this principle. \* \* \*

[343] The effect of these dissimilar conditions upon the amount of tax paid by the coal-mining industry is shown in the analysis of taxes actually paid by the different branches of the mining industry. Such an analysis is contained in the preliminary report on depletion, rendered to the Joint Committee on Internal Revenue Taxation, by L. H. Parker, chief of staff, and by that committee submitted to Congress on September 17, 1929.

\* \* \* These figures are direct and conclusive evidence of the inequitable results of the present statutory provisions relating to depletion and the administrative application of those provisions.

Another indication of the inequitable results of these depletion provisions may be briefly pointed out without comment. From the figures given in the third table on page 8 of Mr. Parker's report it is possible to compute for the single year 1924 the ratio of depletion allowances to gross sales. \* \* \*

[344] Mr. Parker's final conclusion as to the injustices resulting from the practical application of the present depletion provisions, and especially the hardship imposed by them upon the coal industry, deserves to be quoted in full (see p. 22):

In view of the conclusively established injustice inflicted upon the coal mining industry as the result

of present rules and practices relating to mine depletion, your petitioners, speaking on behalf of the bituminous mining industry of the country, feel that they are justified in requesting relief through changes in the income tax law so far as it relates to depletion allowances. We respectfully urge that the present provisions relating to depletion be amended by the insertion of the following paragraph (3) immediately after the present paragraph (2) of section 114 of the revenue act of 1928:

“(3) *Percentage depletion for coal mines.*—In the case of coal mines the allowance for depletion shall be  $33\frac{1}{3}$  percent of net income before depletion; provided that such depletion allowance shall not be less than 5 percent of the gross income from the sale of coal at the mine; and provided, further, that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.”

[345] The proposed amendment provides for an alternative depletion allowance of 5 per cent of gross income from the sale of coal. *The immediate purpose of this provision is to take care of companies producing so-called captive tonnage. Many such companies owned by railroads, electric power plants, steel mills or other industries sell no coal in the open market but deliver their entire output to the parent company. The aggregate amount of such tonnage in the coal mining industry is very large. In many instances the price at which the tonnage is transferred from the subsidiary to the parent company is arbitrarily fixed and bears no relation to current market value. Indeed in some States utilities owning subsidiary coal-mining companies are required by law to take over the tonnage of such subsidiaries at cost. In the case of the last mentioned companies there is no*



figure on the books representing net profit. Unless such companies are to be entirely deprived of depletion allowances provision must be made for computing such allowances on the basis of gross income from the sale of their product. [*Italics supplied.*]

The only alternative method that can be applied to such companies is an arrangement under which the Commissioner of Internal Revenue will set up a constructive net income based upon market conditions at the time and place of the transfer of the product. Arrangements imposing upon the Commissioner the duty of constructive action of this kind have never proven satisfactory. \* \* \* The construction of a theoretical net income for companies producing captive tonnage will prove equally unsatisfactory as a method of arriving at the depletion allowance of subsidiary companies of the kind under consideration.

The provision for an allowance of 5 per cent of gross income will have wider application. Without regard to the effect of the present depression upon the coal-mining industry its financial experience in recent years has been very unsatisfactory. The period 1928 and 1929 to October of the latter year was one of unexampled prosperity for industry in general. Even during those years the coal-mining industry was far from prosperous. The Statistics of Income, issued by the Bureau of Internal Revenue, show that in 1928 two-fifths of the coal-mining companies reported net losses for the year and that the losses so reported exceeded the net income reported by the remaining companies by nearly \$20,000,000; in 1929 nearly two-thirds of the companies reported no net income and the aggregate losses of these companies exceeded the net income of the remaining companies by nearly \$9,000,000. In other words, in those two years the coal-mining industry as a whole not only

had no net income but was substantially in the red.

It is obvious that in a year in which the coal-mining industry as a whole operates at a loss, a depletion allowance computed as a percentage of net income will not be a measure of substantial relief. If in such a period the industry is to be relieved from the inequitable burden of taxation under which it now suffers, its relief can not come solely from a provision giving it a depletion allowance based on net income. Only an allowance computed as a percentage of gross income can adequately meet the situation. \* \* \*

[346] The position of the coal-mining industry with reference to this question of depletion is briefly as follows: The industry has always been and still is the victim of an inequitable distribution of the income-tax burden. \* \* \*

[347] National Coal Association, Washington, D.C.,  
Carroll B. Huntress, executive secretary; \* \* \*

**Senate Hearings, 1932**

(Hearings before the Committee on Finance, United States Senate, 72d Cong., 1st Sess., on H.R. 10236.)

[224] Statement of DONALD A. CALLAHAN, of WALLACE, IDAHO, representing Northwestern Mining Association.

I am not appearing here in opposition to anything in the way of tax, but I am appearing here in support of an amendment which was offered by Senator Thomas of Idaho, and which would provide as the

basis of depletion in metal mines a percentage rate of 15 per cent *of the gross*. [Italics supplied.]

[225] Depletion of mines under our income tax laws means an annual deduction from gross income of an amount which is estimated will compensate the miner for the capital which has been used up or destroyed through the operation of his mine during the year. Obviously all the ore in his mine at the beginning of his operation is capital. Plainly, also, when he takes that ore out of the mine and sells it he has disposed of his capital. Our income tax laws have never attempted to tax him on that portion of the proceeds of his sales which may be regarded as a return of capital. The only question which has been considered in past income tax laws, and which is being considered here, is: "What is the proper method of ascertaining the amount of the proceeds of his sales *of ore* which may be regarded as return of capital and upon which he should pay no tax?" Looking upon it from another angle it may be said that depletion for mines represents the same element as the cost of raw materials in a manufacturing process. [Italics supplied.]

SENATOR BINGHAM. Mr. Chairman, may we have a copy of Senator Thomas's amendment so that we can have it before us? Has it been printed?

The CHAIRMAN. Yes.

(The amendment is as follows:)

Amendment intended to be proposed by Mr. Thomas of Idaho to the bill (H.R. 10236) to provide revenue, equalize taxation, and for other purposes, viz: -

On page 84, line 15, after "for" insert "metal mines,"; and beginning with the word "In" in line 16 strike out through the period in line 19 and insert in

lieu thereof the following: "The allowance for depletion shall be, in the case of metal mines, 15 percent, and in the case of sulphur, oil, and gas wells, 27½ per cent of the gross income from the property during the taxable year."

[226] Mr. CALLAHAN. 1929. The figures that have been compiled by the Joint Committee on Internal Revenue Taxation, and which are contained in the preliminary report that was presented, covers those very figures. It covers them not for one year but over a period of years. In which it is shown that the average of depletion allowed amounted to better than 17 per cent.

SENATOR REED. On gross?

Mr. CALLAHAN. Yes. Those figures are in this preliminary report which was prepared by Mr. Parker and his staff.

[227] Mr. CALLAHAN. \* \* \* Now we are in a different position than we were when these bills were originally written. We have back of us here a world of experience in production and all that sort of thing. We know what the percentage of depletion now would mean as related to what depletion has actually been allowed in the past, and we have purposely placed this even lower than the figure which the weighted average shows at the present time in order that there will be no decrease in revenue, and we contend that there will be an actual increase in the stability of revenue, because \* \* \*

[228] \* \* \*

SENATOR COUZENS. Leaving out of consideration your district, do you think that the 15 per cent is fair to all districts?

Mr. CALLAHAN. I think it is fair to all districts because it is the nearest approach to the average that

we can attain. And I think it is absolutely fair. It is our opinion that it is fair. Never been denied that it was not fair.

SENATOR KING. How can you establish a uniform rule, Mr. Callahan, when you have different conditions in different places? \* \* \* It seems to me it is difficult to establish uniform plans for the purpose of applying the rule of depletion.

Mr. CALLAHAN. It is very difficult. Not only difficult, but absolutely impossible *under the present plan.* [Italics supplied.]

[229] Mr. CALLAHAN. \* \* \*

There are three sources, of course, of opposition to this. \* \* \*

But we are firmly convinced that the application of the percentage method will do away with a large amount of the expense of the department. It will do away with a tremendous amount of expense to the taxpayer in first establishing his valuations and afterwards maintaining them. That it will mean a more stable revenue if it is adopted with the provision that it can not exceed 50 per cent of the net. And it will mean this, that valuations will not be established, as they have been in the past, in times of high prices, when there was a big price for a unit of ore, and then depleted at a time of lower prices. \* \* \*

[230] SENATOR COUZENS. Before you get to that point. The adoption of this plan would put you all on the same basis?

Mr. CALLAHAN. *The adoption of this plan would put us all on the same basis, absolutely.* [Italics supplied.]



SENATOR COUZENS. And these concerns that now have this big advantage taken away?

Mr. CALLAHAN. Yes.

SENATOR KING. It would inure to your advantage in a little way, but to the disadvantage of some others that you think now have an advantage?

Mr. CALLAHAN. No; I do not think it would inure to their disadvantage. No, I do not think it would. I think they imagine it would. And there is also a tendency of those going along in business to say, "Let well enough alone."

The CHAIRMAN. I can not conceive of any mine, unless it was a wild-catter, but that this amendment would be an advantage to.

Mr. CALLAHAN. I think it would. Not in the matter of taking away revenue from the Government, but in the matter of their carrying on their own business.

\* \* \* \* \*

[231] SENATOR REED. Mr. Callahan, what would be your feeling toward basing your depletion upon a percentage of net income instead of gross?

Mr. CALLAHAN. Well, probably we would favor that. *It has been figured out that 15 per cent of gross will amount to about as much as 30 per cent of net. That is the experience. And we would have no objection to figuring it on that basis. [Italics supplied.]*

SENATOR COUZENS. It seems to me that to figure on percentage of net would encourage extravagance.

Mr. CALLAHAN. Yes. This is simpler.

SENATOR COUZENS. Do I understand that if this plan were adopted it would be necessary to eliminate the discovery percentages?

Mr. CALLAHAN. It is not necessary to eliminate, but you gentlemen know and I know that it should be eliminated.

**SENATOR COUZENS.** Would not those who get a discovery allowance have an advantage over you if this plan were adopted and you only got the percentage?

**Mr. CALLAHAN.** It would be an advantage temporarily, perhaps, but it would not be an advantage that would be continuous. And what we are asking is a permanent change of policy with regard to this thing, which we feel will be to the advantage of all mines and will be tremendously to the advantage of the Government.

[232] **May I now say in conclusion that a number of the States have recently adopted income tax laws. Senator Smoot's State of Utah, after a thorough investigation by a commission, adopted an income tax law, and they incorporated in that after their investigation the percentage method of depletion.**

**SENATOR REED.** Based on gross?

**Mr. CALLAHAN.** I do not know whether theirs is based on gross or net.

**The CHAIRMAN.** On net, I think.

**Mr. CALLAHAN.** On net. Our State of Idaho based theirs on net. The State of Oregon and the State of California—all of those that have recently enacted income-tax laws—provided the percentage depletion for mines in their laws.

**SENATOR COUZENS.** On net or gross?

**Mr. CALLAHAN.** Well, I think they are principally on net. I think that that was done in all of them. I know it is in our State.

**SENATOR COUZENS.** Why did they adopt net and you recommend gross?

**Mr. CALLAHAN.** Well, as a matter of fact there has been just a question always as to which is which.

**SENATOR REED.** *As a matter of fact it is based to some extent on both where you say that it shall not exceed 50 per cent net. [Italics supplied.]*

Mr. CALLAHAN. Yes, it is. This, of course, has that saving provision. But, as I say, the estimate from the figures is that this amounts to about 30 per cent on net.

I am filing this statement, Mr. Chairman.

The CHAIRMAN. Very well, (that may be placed in the record.

(The statement presented by Mr. Callahan is here printed in the record, in full, as follows:)

Statement of DONALD A. CALLAHAN, of WALLACE, IDAHO, representing Northwestern Mining Association:

I am appearing in support of the amendment offered by Mr. Thomas of Idaho relative to the allowance for depletion in the case of metal mines.

\* \* \* \* \*

[233] As a result of the administration of this law we find tremendous inequalities between taxpayers who are engaged in the same line of business. \* \* \*

\* \* \* \* \*

[234] Besides these inequities as between different branches of the industry and different districts in which the same metal is produced, there are also tremendous inequalities as between individual taxpayers. \* \* \*

\* \* \* \* \*

[235] \* \* \* There are companies operating to-day that have a depletion valuation per unit for their ore in the ground higher than the price which they receive for their finished product.

Under the percentage plan this could not occur, if the limitation of deduction for depletion be fixed, as it is in this amendment at 50 per cent of net income. Under the present system a taxpayer may show a profit before depletion and wipe it out completely by deple-

tion allowance. Under a straight percentage plan, with a limitation such as in the amendment, he must, in any event, pay upon 50 per cent of that net income.

There is proposed in this amendment a plan by which, instead of the involved processes now employed, the taxpayer may deduct 15 per cent of his gross income, provided it does not exceed 50 per cent of his net income. There will be no valuations, no estimates, no predictions. It is the same principle as was applied by Congress to the oil and gas industry, with a different rate because of the difference in the nature of the two industries.

The question may be asked "Why the rate of 15 per cent of gross?" That rate has been determined as one which, according to actual experience will amount to less than the average of depletion which has been allowed in the past. These figures are given in the Parker report, heretofore referred to, at page 67. I think it is agreed as between the Bureau of Internal Revenue and the mining industry that the average of depletion allowance has been above 17 per cent of gross. The amendment here offered, therefore, will result not in a lessening, but in an increase of revenue, and because of the fact that not more than 50 per cent of net can be deducted will, in my judgment, result in a considerable increase and a much more stable income to the Government.

[236] Brief submitted by National Coal Association and District Association of Bituminous Mine Operators.

# PERCENTAGE DEPLETION ALLOWANCE FOR BITUMINOUS COAL MINES

TO THE FINANCE COMMITTEE,  
*United States Senate, Washington, D.C.*

[This brief, which appears on pages 236-242, is identical to the one submitted during the hearings before the Ways and Means Committee, portions of which are printed *supra*, pp. 117-122.]

S. Rep. No. 665

(72d Cong., 1st Sess., pp. 16, 30: (1939-1 Cum. Bull. (Part 2) 496, 507))

#### Sec. 23(1). DEPLETION.

\* \* \* \* \*

The cross reference contained in the House bill to section 114(b)(3) relating to percentage depletion is changed in view of the fact that percentage depletion has been extended to metal mines as well as to sulphur and oil and gas wells.

\* \* \* \* \*

#### Sec. 114. BASIS FOR DEPLETION.

The amendment to paragraph (b)(2) as contained in the House bill makes it clear that in the case of metal and sulphur mines the depletion allowances may not longer be computed upon the basis of discovery value.

Paragraph (b)(3) of the House bill has been amended by the elimination of the word "sulphur" to restrict the application of the paragraph to oil and gas wells.

#### Sec. 114(b)(4). PERCENTAGE DEPLETION FOR METAL MINES AND SULPHUR.

Under paragraph (b)(4) metal mines are granted a percentage depletion allowance of 15 per cent, and sulphur mines or deposits of 23 per cent of *the gross income from the property* during the taxable year. As in the case of oil and gas wells this allowance can not exceed 50 per cent of the net income of the taxpayer from the property. In respect to the taxable years 1932 and 1933 the taxpayer is privileged to have



the greater of either (1) the percentage depletion allowance or (2) an allowance computed on the adjusted basis provided in section 113(b) (usually cost or March 1, 1913, value, with adjustments). This privilege is the same for those two years as that accorded both under the existing law and the bill in the case of oil and gas wells for all years. [Italics supplied.]

In the return for the taxable year 1933, however, the taxpayer is required to state as to each property whether he elects to have the depletion allowance for such property for succeeding taxable years computed with or without reference to percentage depletion; this election must be as between either percentage depletion or depletion computed upon the adjusted basis. In the case of any property in respect of which a return is first made in a year subsequent to the taxable year 1933, the election indicated in the return for such year shall be binding as to all future years. If the taxpayer fails to make such election in the return in which it should be indicated, the depletion allowance for that and succeeding taxable years will be computed on the adjusted basis.

H. Conference Rep. No. 1492

(72d Cong., 1st Sess. (1939-1 Cum. Bull. (Part 2) 539))

[14] AMENDMENT No. 54: This amendment changes the rate of percentage depletion in the case of sulphur from 27½ per cent, as in the House bill, to 23 per cent, of the *gross income from the property*, and allows percentage depletion in the case of coal and of metal mines, at the respective rates of 5 per cent and 15 per cent of the *gross income from the property*; the percentage depletion allowance can not in any

case exceed 50 per cent of the net income from the property. As in the case of oil and gas wells the amendment makes it clear that rents and royalties paid or incurred by the taxpayer in respect of the property are to be excluded in computing the gross income from the property. The amendment requires that the taxpayer make in his 1933 return an election, binding for 1934 and subsequent years, whether he will have the depletion deduction as to each property computed with or without reference to percentage depletion, and the failure so to elect will preclude the use of percentage depletion. The amendment also provides that if, because of the provisions of section 113(a) of the bill, the basis of property acquired after December 31, 1933, is determined either (1) by reference to the basis of the property in the hands of a transferor, donor, or grantor or (2) by reference to the basis of other property previously held by the taxpayer, then the method of computing the depletion allowances in respect of the property so acquired, shall be the same as the method previously used by the transferor, donor, or grantor, or by the taxpayer in [15] respect of the property previously held. The House recedes with a clerical amendment. [Italics supplied.]

\* \* \* \* \*

Revenue Act of 1932

(c. 209, 47 Stat. 169)

**SEC. 23. DEDUCTIONS FROM GROSS INCOME.**

In computing net income there shall be allowed as deductions:

\* \* \* \* \*

(1) *Depletion*.—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in

each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. \* \* \* In the case of leases the deductions shall be equitably apportioned between the lessor and lessee. \* \* \* (For percentage depletion, see section 114(b) (3) and (4).)

(m) *Basis for Depreciation and Depletion.*—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114.

SEC. 114. BASIS FOR DEPRECIATION AND DEPLETION.

(a) *Basis for Depreciation.*—\* \* \*

(b) *Basis for Depletion.*—

(1) *General Rule.*—The basis upon which depletion is to be allowed in respect of any property shall be the adjusted basis provided in section 113(b) for the purpose of determining the gain or loss upon the sale or other disposition of such property, except as provided in paragraphs (2), (3), and (4) of this subsection.

(2) *Discovery value in case of mines.*—\* \* \*

(3) *Percentage depletion for oil and gas wells.*—  
In the case of oil and gas wells the allowance for depletion shall be  $27\frac{1}{2}$  per centum of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance be less than it would be if computed without reference to this paragraph.

(4) *Percentage depletion for coal and metal mines and sulphur.*—The allowance for depletion shall be, in the case of coal mines, 5 per centum, in the case of metal mines, 15 per centum, and, in the case of sulphur mines\* or deposits, 23 per centum, of the *gross income from the property* during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. [Italics supplied.] Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance for the taxable year 1932 or 1933 be less than it would be if computed without reference to this paragraph. A taxpayer making return for the taxable year 1933 shall state in such return, as to each property (or, if he first makes return in respect of a property for any taxable year after the taxable year 1933, then in such first return), whether he elects to have the depletion allowance for such property for succeeding taxable years computed with or without reference to percentage depletion. The depletion allowance in respect of such property for all succeeding taxable years shall be computed according to the election thus made. If the taxpayer fails to make such statement in the return, the depletion allowance for such property for succeeding taxable years shall be computed without reference to percentage depletion. During the period for which property acquired after December 31, 1933, is held by the taxpayer—

(A) if the basis of the property in the hands of the taxpayer is, under section 113(a), determined by reference to the basis in the hands of the transferor, doner, or grantor, then the depletion allowance in respect of the property shall be computed with or without reference

to percentage depletion, according to the method of computation which would have been applicable if the transferor, donor, or grantor had continued to hold the property, or

(B) if the basis of the property is, under section 113(a), determined by reference to the basis of other property previously held by the taxpayer, then the depletion allowance in respect of the property shall be computed with or without reference to percentage depletion, according to the method of computation which would have been applicable in respect of the property previously held if the taxpayer had continued to hold such property.

**Treasury Regulations 77**

(Released February 10, 1933)

**ART. 221.** Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.— \* \* \*

When used in these articles (221-248) covering depletion and depreciation—

(g) "Gross income from the property" as used in section 114(b) (3) and (4) and articles 221 to 248, inclusive, means the amount for which the taxpayer sells (a) the crude mineral product of the property or (b) the product derived therefrom, not to exceed in the case of (a) the representative market or field price (as of the date of sale) of crude mineral product of like kind and grade before transportation from the immediate vicinity of the mine or well, or in the case of (b) the representative market or field price (as of the date of sale) of a product of like kind and grade from which the product sold was derived, before the application of any processes (to which the crude mineral product may have been subjected after emerging



from the mine or well) with the exception of those listed below, and before transportation from the place where the last of the processes listed below was applied. Where there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes minus the costs (including transportation costs) of the processes not listed below. The processes excepted are as follows:

(1) In the case of coal—cleaning, breaking, sizing, and loading at the mine for shipment;

(2) In the case of sulphur—pumping to vats, cooling, breaking, and loading at the mine for shipment;

(3) In the case of iron ore and ores which are customarily sold in the form of the crude mineral product—sorting or concentrating to bring to shipping grade, and loading at the mine for shipment; and

(4) In the case of lead, zinc, copper, gold, or silver ores and ores which are not customarily sold in the form of the crude mineral product—crushing, concentrating (by gravity or flotation), and other processes to the extent to which they do not beneficiate the product in greater degree (in relation to the crude mineral product on the one hand and the refined product on the other) than crushing and concentrating (by gravity or flotation).

In all cases there shall be excluded in determining the "gross income from the property" an amount equal to any rents or royalties which were paid or incurred by the taxpayer in respect of the property and are not otherwise excluded from the "gross income from the property." Where royalties in the form of bonus payments or advanced royalties (see article 230) have been paid in respect of the property in the taxable

year or in prior years, the amount excluded from "gross income from the property" for the taxable year on account of such payments shall be an amount equal to that part of such payments which is allocable to the *products* sold during the taxable year. [*Italics supplied.*]

(h) "Net income of the taxpayer (computed without allowance for depletion) from the property," as used in section 114(b) (2), (3), and (4) and articles 221 to 248, inclusive, means the "gross income from the property" as defined in paragraph (g) less the allowable deductions attributable to the mineral property upon which the depletion is claimed and the allowable deductions attributable to the processes listed in paragraph (g) in so far as they relate to the product of such property; including overhead and operating expenses, development costs properly charged to expense, depreciation, taxes, losses sustained, etc., but excluding any allowance for depletion. Deductions not directly attributable to particular properties or processes shall be fairly allocated. To illustrate: In cases where the taxpayer engages in activities in addition to mineral extraction and to the processes listed in paragraph (g), deductions for depreciation, taxes, general expenses, and overhead, which can not be directly attributed to any specific activity, shall be fairly apportioned between (1) the mineral extraction and the processes listed in paragraph (g) and (2) the additional activities, taking into account the ratio which the operating expenses directly attributable to the mineral extraction and the processes listed in paragraph (g) bear to the operating expenses directly attributable to the additional activities. Where more than one mineral property is involved, the deductions apportioned to the mineral extraction and the processes listed in paragraph (g) shall, in turn, be fairly

apportioned to the several properties, taking into account their relative production.

(i) "Crude mineral product," as used in paragraphs (g) and (h) of this article, means the product in the form in which it emerges from the mine or well.

1934

[In its proposals for the Revenue Act of 1934, c. 277, 48 Stat. 680, the Treasury Department recommended elimination of discovery and percentage depletion. Representatives of the mining industry appeared before the House Ways and Means Committee in opposition to these proposals. Illustrative portions of their testimony follow.]

House Hearings, 1934

(Revenue Revision, 1934, Hearings before the Committee on Ways and Means, House of Representatives, 73d Cong., 2d Sess.)

[266] Statement of LOUIS C. GRATON, Cambridge, Mass., representing the Cerro de Paseo Copper Corporation:

[271] Beyond what I have already said, the arguments in favor of percentage depletion when properly determined are so numerous and voluminous as to make at once impossible and improper their complete inclusion before your committee assembled in session. Furthermore, they inevitably involve many considerations of a specialized technical nature, adequate illumination of which would entail extended explanation and long chains of close reasoning that would be difficult to follow in oral presentation. *The entire subject has been very fully covered, however, in official documents, notably the "Preliminary Re-*

*port on Depletion", submitted in 1929 to the Joint Committee on Internal Revenue Taxation by its technical staff under the direction of Mr. L. H. Parker; and, second, the fuller record entitled "Depletion of Mines", presented at the hearings before the joint committee in 1930. If permissible, I should like to submit also an article entitled "Percentage depletion for mines", presented before the American Mining Congress in 1929, and now marked "Exhibit A." [Italics supplied.]*

[392] Statement of DONALD A. CALLAHAN, of Wallace, Idaho, representing the Northwest Mining Association:

The CHAIRMAN. Give your name and address, Mr. Callahan.

Mr. CALLAHAN. My name is Donald A. Callahan. My address is Wallace, Idaho.

Mr. Chairman and members of the committee: I am here to represent the Northwest Mining Association, a group of those engaged in the metal-mining industry in the Northwest; and also, as Mr. Fernald has stated, to represent the views generally of the American Mining Congress, particularly with relation to the question of mine depletion as it particularly applies to metal mining.

[393] In 1929 the staff of the Joint Committee on Internal Revenue Taxation presented a preliminary report to this committee, and in that report it used the following language:

Following the submission of this report a hearing was had before the Joint Committee in 1930, and the results and the record of that hearing, of course, are available to the members of this committee.

The principle of percentage depletion had been applied to oil and gas wells in the Revenue Act of 1926, and has been in effect in that industry ever since. In 1932 it was extended to metal mines, sulphur, and coal, the allowance for metal mines being 15 percent of gross. This action was taken by the Congress after a hearing before the Senate Committee on Finance and with all the data contained in the report of the staff of the Joint Committee on Internal Revenue Taxation and of the hearings before that committee available for its consideration. It was a matured and reasoned decision upon the part of Congress. It was a step taken to do away with inequalities that had been manifest in the administration of the law as theretofore existing. That step was also prompted by a desire to do away with high administration costs and to return a more stable revenue to the Government. It was not intended as a subsidy, but as a correction of evils which had grown up under a system that was exceedingly difficult and costly to administer.

[397] Statement of E. T. CUMMINS, representing American Sulphur Producers, Washington, D.C.:

The subject we are interested in has been covered very well by Mr. Fernald and Mr. Callahan, who appeared before the committee this morning; and in order to save time I would just like to ask permission to file a statement in the record.

The CHAIRMAN. Without objection, that may be done.

(The statement referred to follows:)



WASHINGTON, D.C., *December 20, 1933.*

*Chairman and Members of the Ways and Means Committee of the House of Representatives.*

[398] That the percentage depletion rate which Congress, after the most exhaustive investigation, established for the sulphur industry in the Revenue Act of 1932 is fair and reasonable and should not be disturbed.

In fixing the rates of percentage depletion contained in the Revenue Act of 1932 each branch of the mining industry was made the subject of a separate study. In each case the joint congressional Committee on Internal Revenue Taxation took into account the facts developed over long periods of time. In the course of these investigations the sulphur industry was subjected to a most exhaustive study and as a result of the studies, the committee aforesaid recommended a rate which is regarded as fair and proper to the industry. This rate was adopted and approved by Congress in the Revenue Act of 1932.

In conclusion, the principle of percentage depletion as applied to the sulphur industry rests upon sound economic principles and the rate applied to that industry represents a fair and reasonable allowance. It is, therefore, respectfully submitted that the principle and rate established in the Revenue Act of 1932 be continued.

Respectfully submitted.

FREEPORT SULPHUR Co.,  
New York, N.Y.

1936.

[Section 114(b)(4) of the Revenue Act of 1936, c. 690, 49 Stat. 1648, merely made a change regarding election of the manner of taking depletion.]

So far as pertinent here, Treasury Regulations 94, promulgated under the 1936 Act, are the same as those promulgated under the 1934 Act except that Article 23(m)-1(3)(g) added the following:

\*     \*     \*     \*

In the case of oil and gas, if the crude mineral product is not sold on the property but is manufactured or converted into a refined product or is transported from the property prior to the sale, then the "gross income from the property" shall be assumed to be equivalent to the market or field price of the oil or gas before conversion or transportation.

1940

[As in the 1934 and 1936 Acts, the material provisions relating to percentage depletion remained substantially the same in the Revenue Act of 1938, c. 289, 52 Stat. 447, and were adopted in the Internal Revenue Code of 1939. Similarly, the Treasury Regulations remained basically unchanged until January 1940, when the "proportionate profits test" was first introduced by the issuance of T.D. 4960, approved January 3, 1940 (1940-1 Cum. Bull. 38), amending Treasury Regulations 101, which had been made applicable to the Internal Revenue Code of 1939 by T.D. 4885 (1939-1 Cum. Bull. (Part 1) 396). As contained in Treasury Regulations 103, issued in 1940, the pertinent sections are given below.]

**Treasury Regulations 103 (1940 ed.)**

(Promulgated under the Internal Revenue Code of 1939)

**SEC. 19.23(m)-1. *Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.***—Section 23(m) provides that there shall be allowed as a deduction in computing net income in the case of mines, oil and gas wells, other

natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements. Section 114 prescribes the bases upon which depreciation and depletion are to be allowed.

Under such provisions, the owner of an economic interest in mineral deposits or standing timber is allowed annual depletion deductions. An economic interest is possessed in every case in which the taxpayer has acquired, by investment, any interest in mineral in place or standing timber and secures, by any form of legal relationship, income derived from the severance and sale of the mineral or timber, to which he must look for a return of his capital. But a person who has no capital investment in the mineral deposit or standing timber does not possess an economic interest merely because, through a contractual relation to the owner, he possesses a mere economic advantage derived from production. Thus, an agreement between the owner of an economic interest and another entitling the latter to purchase the product upon production or to share in the net income derived from the interest of such owner does not convey a depletable economic interest.

The adjusted basis of depreciable property is returnable through annual depreciation deductions. Depreciation and depletion deductions on the property of a corporation are allowed to the corporation and not to its shareholders. (But see section 19.115-6.) The principles governing the apportionment of depreciation in the case of property held by one person for life with remainder to another person and in the case of property held in trust are also applicable to depletion. (See section 19.23(1)-1.)

When used in these sections (19.23(m)-1 to 19.23(m)-28, inclusive) covering depletion and, depreciation—

(a) The "fair market value" of a property is that amount which would induce a willing seller to sell and a willing buyer to purchase.

(b) A "mineral property" is the mineral deposit, the development and plant necessary for its extraction, and so much of the surface of the land only as is necessary for purposes of mineral extraction. The value of a mineral property is the combined value of its component parts.

(c) The term "mineral deposit" refers to minerals in place. The cost of a mineral deposit is that proportion of the total cost of the mineral property which the value of the deposit bears to the value of the property at the time of its purchase.

(d) "Minerals" include ores of the metals, coal, oil, gas, and such nonmetallic substances as abrasives, asbestos, asphaltum, barytes, borax, building stone, cement rock, clay, crushed stone, feldspar, fluorspar, fuller's earth, graphite, gravel, gypsum, limestone, magnesite, marl, mica, mineral pigments, peat, potash, precious stones, refractories, rock phosphate, salt, sand, silica, slate, soapstone, soda, sulphur, and talc.

(e) The term "mine" does not include oil and gas wells.

(f) "Gross income from the property," as used in section 114(b) (3) and (4) and sections 19.23(m)-1 to 19.23(m)-28, inclusive, means the amount for which the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine or well, but, if the product is transported or processed (other than by the processes excepted below) before sale, it means the representative market or field price (as of the date of sale) of crude mineral product of like kind and grade before such transportation or processing. If there is no such representative market or field price (as of the date of sale), then there

shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation and the processes not listed below. The processes excepted are as follows:

(1) In the case of coal—cleaning, breaking, sizing, and loading at the mine for shipment;

(2) In the case of sulphur—pumping to vats, cooling, breaking, and loading at the mine for shipment;

(3) In the case of iron ore and ores which are customarily sold in the form of the crude mineral product—sorting or concentrating to bring to shipping grade, and loading at the mine for shipment; and

(4) In the case of lead, zinc, copper, gold, or silver ores and ores which are not customarily sold in the form of the crude mineral product—crushing, concentrating (by gravity or flotation), and other processes to the extent to which they do not beneficiate the product in greater degree (in relation to the crude mineral product on the one hand and the refined product on the other) than crushing and concentrating (by gravity or flotation).

In case any of the excepted processes are not applied in the immediate vicinity of the mining district in which the mine is located, costs incurred for transportation to the processing location and, if transported by taxpayer, the proportionate profits attributable to transportation should be subtracted from the sale price of the product to determine "gross income from the property."

In the case of oil and gas, if the crude mineral product is not sold on the property but is manufac-



tured or converted into a refined product or is transported from the property prior to the sale, then the "gross income from the property" shall be assumed to be equivalent to the market or field price of the oil or gas before conversion or transportation.

\*     \*     \*     \*     \*

(g) "Net income of the taxpayer (computed without allowance for depletion) from the property," as used in section 114(b) (2), (3), and (4) and sections 19.23(m)-1 to 19.23(m)-28, inclusive, means the "gross income from the property" as defined in paragraph (f) of this section less the allowable deductions attributable to the mineral property upon which the depletion is claimed and the allowable deductions attributable to the processes listed in paragraph (f) in so far as they relate to the product of such property, including overhead and operating expenses, development costs properly charged to expense, depreciation, taxes, losses sustained, etc., but excluding any allowance for depletion. Deductions not directly attributable to particular properties or processes shall be fairly allocated. To illustrate: In cases where the taxpayer engages in activities in addition to mineral extraction and to the processes listed in paragraph (f), deductions for depreciation, taxes, general expenses, and overhead, which cannot be directly attributed to any specific activity, shall be fairly apportioned between (1) the mineral extraction and the processes listed in paragraph (f) and (2) the additional activities, taking into account the ratio which the operating expenses directly attributable to the mineral extraction and the processes listed in paragraph (f) bear to the operating expenses directly attributable to the additional activities. If more than one mineral property is involved, the deductions apportioned to the mineral extraction and

the processes listed in paragraph (f) shall, in turn, be fairly apportioned to the several properties, taking into account their relative production.

(h) "Crude mineral product," as used in paragraph (f) of this section, means the product in the form in which it emerges from the mine or well.

\* \* \* \* \*

1942

[In the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 145, fluorspar, ball and sagger clay, and rock asphalt were granted a 15 percent depletion allowance. Through its representatives, the mining industry appeared before the Ways and Means Committee, the Senate Finance Committee and a subcommittee of the Senate Special Committee on the Investigation of Silver where various problems, including the definition of gross income from the property and the propriety of the "proportionate profits test", were discussed. Pertinent extracts from these hearings, the Committee reports, Congressional debates, and the Act as passed are printed below in chronological order.]

House Hearings, 1942

(Revenue Revision of 1942, Hearings before the Committee on Ways and Means, House of Representatives, 77th Cong., 2d Sess.)

[1168] Statement of DONALD A. CALLAHAN, Wallace, Idaho, vice president, American Mining Congress:

\* \* \* \* \*

[1169] Mr. CALLAHAN. \* \* \* \*

Another thing that enters into the production of metals is that in the gross price that is finally paid for the metals there is included so much for elements of the cost that do not enter into the matter of oil and gas. Those are included in the price that is eventually

[1170] received for the metals. That accounts for the difference in the percentage.

As a matter of fact, *this whole matter of percentage depletion was so thoroughly reviewed by the Joint Committee on Internal Revenue Taxation and by the committees when percentage depletion was extended to mines that I can do nothing better than refer you to the report, which I see you have had reprinted; and that is the report of the staff of the Joint Committee on Internal Revenue Taxation, made before this allowance of percentage depletion for mines was written into the law.* [Italics supplied.]

*It was upon this largely that the committees of Congress acted in doing away with discovery depletion as it related to mines, and substituted therefor the method of depletion according to this percentage.* [Italics supplied.]

They arrived at that percentage by taking the average of the depletion allowance under the old method hitherto in vogue and which had been used from the very beginning, taking the weighted average over a 5-year period, and finding that that amounted for metal mines to a little better than 17 per cent of the net smelter return, which was the selling price of the ore. They also found that that amounted to approximately  $33\frac{1}{3}$  per cent of the net, which was the rate then employed in Canada.

The rate of 15 per cent was agreed upon more or less as a compromise, which was less than the average rate that had been paid over that weighted period, and which amounted to approximately 30 percent of the net value.

[1182] I have here certain memoranda in regard to this percentage depletion of mines which I would like

to file for the record. They illustrate certain points that I have brought out.

The CHAIRMAN. Without objection, that may be filed.

(The memoranda referred to are as follows:)

[1184]

# PERCENTAGE DEPLETION—THE POSITION OF THE MINING INDUSTRY

By the American Mining Congress, Washington, D.C., March 1942

The Secretary of the Treasury and the special tax adviser to the Treasury have made certain statements and advanced certain recommendations to the Ways and Means Committee of the House of Representatives touching the allowances for depletion in case of metal mines. These statements and recommendations may be briefly summarized as follows:

We summarize the position of the mining industry briefly as follows:

1. *Depletion is a return to the mining industry of the capital consumed in its operations.*—The mineral in place in the ground is the principal capital of every mineral producer. As each ton is extracted, a certain portion of his capital is actually consumed. A portion of his proceeds from each ton is the return of his capital, and only a portion is income. Since the inception of the income tax, every effort has been made to tax income only and to avoid taxing capital. Depletion is merely the method by which the return of capital is computed. The right to a return of capital has always been recognized. This right has never been seriously questioned. It is not questioned by the Secretary at this time.

2. *The present system of computing depletion resulted from careful study and affords the best means for determining the annual consumption of capital.*—After years of experience with other methods of computing depletion, the Congress in 1932 included the present percentage method for metal mining, coal, and sulfur. This was upon the recommendation of the staff of the Joint Committee on Internal Revenue Taxation, which made an exhaustive study of the subject. The Joint Committee held extensive hearings, and the printed reports of the staff of the Joint Committee and of the hearings before the committee were considered by the Congress in the adoption of the percentage method and in fixing the rates. The rates so fixed were lower than the average rates actually allowed under the previous laws.

3. *The percentage method furnishes both uniformity and certainty in computing depletion.*—The report of the staff of the Joint Committee called special attention to the uncertainty and lack of uniformity under the methods of computing depletion which theretofore had been the only methods allowed. Tables were given showing the wide difference in allowances of depletion between [1185] different branches of the industry and individual taxpayers. The inclusion of the percentage method has remedied this situation.

\*   \*   \*   \*

5. *Percentage depletion provides more equal treatment to those engaged in the industry.*—One of the objects sought to be attained by the percentage method was the elimination of the inequality which had existed as between competing members of the mining industry. Under the methods in use prior to 1932, certain companies had been able to establish adequate depletion allowances which, by reason particularly



of the geological nature of their deposits, were not available under the statute to others. The present law tends to remove this inequality and to give all mining taxpayers some measure of protection against taxation of their capital.

\* \* \* \* \*

7. *Percentage depletion protects the small operator.*—The small mine operator cannot afford to spend the money necessary to establish the value of his mineral deposits and the corresponding depletion value of his unit of production. Percentage depletion removes the necessity for such expenditures. It provides a simple, understandable method by which, from the inception of his enterprise, he may receive the reasonable allowance for depletion contemplated by the statute. It assures him fair and equal treatment with other operators. It protects him against the taxation of the capital he has consumed in his operation.

[1196]

\* \* \* \* \*

Statement of ROBERT M. SEARLS, San Francisco, Calif., representing California Chapter of the American Mining Congress.

\* \* \* \* \*

[1199] *I may go one step further and point out to the committee that the Treasury, in the opinion of the mining industry, has not fairly interpreted the intent of Congress in administering the existing law. The existing law, section 114(b)(4), provides for an allowance of 15 percent of "the gross income from the property during the taxable year" excluding rents and royalties with a further proviso that this 15 percent shall not exceed 50 percent of the net income computed without allowance for depletion. In view of the fact that the gross income of mineral properties has always been considered as the price at which the metals produced can be sold, we submit*

*that it was obviously the intent of Congress that the net mint or smelter value of metals, less possibly the cost of transportation, should be considered as the true gross income of the properties whether these metals are sold in metallic form or in the form of concentrates which are valued solely on the basis of their metal content. The Treasury however has taken the position that the gross income is to be based on what they term "the first marketable product" and if the mine owner instead of erecting a smelter or cyanide plant should sell his metal concentrates to a smelter on the basis of the metal content then, so the Treasury says, the gross income from the property is simply the market value of the concentrates. Then they go a step further, and say, that even if the owner has on the property a smelter or cyanide plant by which to extract the metal from the concentrates the cost of so doing plus an assumed profit on the operation must be subtracted from his gross income in computing depletion because if he did not have these facilities he would have to sell the concentrates. In the case of mercury recently they have gone even further. Cinnabar, the ore from which this metal is produced, has no market as such, and must be beneficiated through roasting in a furnace from which the mercury emerges in vapor is passed into a condenser and emerges in its normal liquid condition. The Treasury proposes to deduct the entire cost of furnacing, for what reason it is not apparent. [Italics supplied.]*

[1202] Recently in the quicksilver mining, where the ore is put directly into the furnace and melted and the quicksilver vapors come off and are condensed and you get the quicksilver without any milling, do we deduct the entire furnace cost on the theory that that is the same kind of processing as cyanide, although the ore from which the metal comes has no market

as such? It has to be transported to market and put up in flasks.

Mr. BUCK. I was somewhat astonished at that statement about quicksilver. After all, the money expended for the production and refining of the cinnabar is a cost, isn't it?

Mr. SEARLS. It is a cost.

Mr. BUCK. Is there any income until it has been refined?

Mr. SEARLS. No, sir; not a dollar, not a dime. And these mines, all of them in California, are 50 or 60 miles from the nearest railroad.

Mr. BUCK. They happen to be in my district.

Mr. SEARLS. Yes; some of them are. One of the oldest and largest of the mines, I think, is in your district.

*The cinnabar, as I say, could not possibly be sold. Yet the Treasury, by the Treasury ruling, insists upon deducting a very considerable cost of milling before getting at the gross revenue from the material. [Italics supplied.]*

I mention these incidents merely to show that percentage depletion is being applied with very rigid adherence to a technical interpretation, and with the 50 percent limit on your net which comes before the 15 percent.

\* \* \* \* \*

H. Rep. No. 2333

(77th Cong., 2d Sess. (1942) (1942-2 Cum. Bull. 372))

[63] DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL

\* \* \* \* \*

[92] SEC. 131. PERCENTAGE DEPLETION FOR COAL,  
FLUORSPAR, AND METAL MINES AND SULPHUR

This amendment provides that fluorspar mines are to be allowed percentage depletion at a rate of 15 per cent, subject to the same limitations as are applicable in the case of metal mines. For taxable years beginning after December 31, 1941, the depletion deduction for coal, fluorspar, metal, and sulphur mines may be computed (without regard to any election) either on the percentage basis or on the cost basis, whichever gives the greater deduction.

Silver Subcommittee Hearings, 1942

(Silver, Hearings before a Subcommittee of the Special Committee on the Investigation of Silver; United States Senate, 77th Cong., 2d Sess., pursuant to S. Res. 187 (74th Cong.) (part 9))

[731]

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Statement of JULIAN D. CONOVER, Mining Engineer,  
Secretary of the American Mining Congress, Washing-  
ton, D.C.:

[736]

6. Depletion.

\* \* \* \* \*

Further, we protest against recent rulings of the Bureau of Internal Revenue tending to curtail the depletion allowances intended by Congress through the Bureau's interpretation of the "gross income from the property," on which the percentage allowance is computed. This adversely affects producers of gold and

silver by the cyanide process, mercury producers, and many others whose ore treatment facilities extend beyond mere crushing and concentration by gravity or flotation methods. I shall not discuss this in detail, but ask your careful consideration of what may be said on the subject.

[738] Statement of ROY A. HARDY, Consulting Mining Engineer for Getchell Mine, Inc., Humboldt County, Nev.

[740]

*In the last few years, the Treasury Department has, in practically all instances, taken an opposite position to that which they have followed for the past 15 or 20 years, and, in the case of depletion where the mining operator felt that a certain policy was being followed, he now finds that the Treasury Department is attempting to upset what has been considered to be a definite depletion procedure and is decidedly unsympathetic. [Italics supplied.]*

[741]

SENATOR MURDOCK. That is, you are constantly depleting what is the capital of the mining company or the individual. Now, would you say that the smelter or the concentration mill which is operated separately from any mines should be so treated, or should they be in an entirely different category for tax purposes?

Mr. HARDY. That would depend on whether it were for custom work entirely or a particular property.

Senator MURDOCK. I am assuming that they are



erected originally for custom work without any particular relationship at all to any specific mine.

Mr. HARDY. Yes; because they should be depleted with a certain rapidity depending on the area from which they are drawing their ores.

SENATOR MURDOCK. *But if we grant to the mine operators that percentage depletion that is now granted to them, or if we increase it, you still think that the smelter or the custom mill should be entitled to a percentage depletion, is that right?* [Italics supplied.]

Mr. HARDY. I do; yes.

SENATOR MURDOCK. *And then, following this line of question, I assume that you take the position that if you have a mine concentration mill and smelter combined that is all owned by one company, operated by that same company, that the depletion should be fixed as against the gross income of the complete operation. Do I make myself clear?* [Italics supplied.]

Mr. HARDY. Certainly. *The Treasury Department takes the opposite view. They say a profit is derived from a part of the process.* [Italics supplied.]

SENATOR MURDOCK. That is the point I would like to have you discuss. It was brought out this morning by Mr. Conover that the internal revenue people had, in his opinion, as I understood him, misconstrued the law and that at certain point in such an operation they want to draw the line and say this is mining up to this point, and entitled to the percentage depletion, but beyond this step in the complete process they are not entitled to it.

Mr. HARDY. It is just like the rancher raising cattle to sell. He feeds the steer hay. Does the Treasury Department say he should [742] pay a profit on the hay as well as on the sale of the steer after the hay has been fed to the cattle? He only has one profit and that is the sale of the steer at the end. Why not

combine that and pay his profit tax on that steer? It is not part of the process of raising that steer. The same thing holds in the mining industry. It is just part of the making of a salable product.

SENATOR MURDOCK. *It is your position, based on your long mining experience, that if you have that combination of mining and processing that the percentage depletion should be figured against the gross income from the completed product?* [Italics supplied.]

Mr. HARDY. Yes; certainly it is.

SENATOR MURDOCK. *Now, if that is allowed, or if that would be allowed, by the Internal Revenue Bureau instead of cutting it off at a certain place, would you be discriminating against, say, the small operator that merely produces ore from his mine and then sells the raw ore to some custom smelter?* [Italics supplied.]

Mr. HARDY. No; there would be no discrimination because his product has to be in a salable form for him to get his profit. When he sells his ore that is figured in his sales.

SENATOR MURDOCK. *In other words, let's see if you will agree with me in this: It is your opinion, then, based on your long mining experience, that a big operator should not be penalized simply because he is able to combine the mining, milling, and smelter under one corporation?* [Italics supplied.]

Mr. HARDY. He should not be penalized; no.

SENATOR MURDOCK. *And that it is no discrimination against the small operator to treat them both in the same category simply because he is too small and not able to combine the milling and smelting with his mine; is that right?* [Italics supplied.]

Mr. HARDY. That is right; yes.

The CHAIRMAN. Are there any further questions?

Mr. L. P. ANDRESEN. Mr. Hardy, among your recommendations is one that the limitation of percentage depletion which is now provided in the act at 50 percent of the net income from the property, be eliminated?

Mr. HARDY. As a straight percentage depletion granted.

Mr. ANDRESEN. Wouldn't that have the effect of completely relieving the mining operator from all taxation where the depletion allowance was exactly equal to the net income?

Mr. HARDY. Mr. Semenza, could you help me out on that question?

Mr. LAURENCE SEMENZA (certified public accountant, Reno, Nev.)—It would have that effect, Mr. Andresen, if the situation should exist some time.

Mr. ANDRESEN. Would not that relieve the taxpayers at this time of great need for revenue of any liability to pay taxes?

Mr. HARDY. It may, in a specific problem, but I could not see that it would in general. What do you think, Mr. Semenza?

Mr. SEMENZA. I can see in a specific case that it might.

[758]

Statement of ROBERT M. SEARLS, Attorney at Law, San Francisco, Calif.:

My name is Robert M. Searls and I am a practicing lawyer in San Francisco, Calif. I have practiced law for more than 30 years, principally in the realm of mines and oil.

[760] Very well. Congress said in section 114(b) (4) that with mineral properties that should be 15

percent of the gross income from the property, and personally I am not quarreling about the percentage. \* \* \* But what I am coming to, *what I term the "chiseling" of the original intent of Congress through administrative measure, is this:* Now, section 23 (m) provides that the depletion should be computed according to peculiar conditions in each case under regulations to be prescribed by the Commissioner of Internal Revenue. Then that was modified by section 114, to which I referred before, saying that this percentage in the case of metal mine incomes should be limited to 15 percent, but that is the only extent to which it was modified. Under the authority of that section, the Treasury has promulgated its regulations. Treasury Regulation 103, section 19.23(m), is the one that was apparently most pertinent here. I will read a short excerpt from it, as follows: [Italics supplied.]

\* \* \* \* \*

Now, I submit that a mineral property has no value at all, with which we are concerned here, except for the metal which it contains. If you are a small operator and sell your concentrates to a smelter instead of producing them yourself or beneficiating the concentrates or not, the valuable product itself is the metal in them. It is true sometimes concentrates are put into a steel furnace with other ores and turned into alloy steels by proper measurement, but it is the metal that is the thing of value, not the rock, sand, gravel, silica, or what not, that gives it the value; it is the metal. *Therefore I say it was the intent of Congress when they said "gross income from the property" meant gross value of the metal from the property.* I say further if they mean gross value, there is no more fair ground for deducting the cost of concentrating, cyaniding, or milling that ore, or even roasting it in the case of quicksilver, than there is for deducting the

cost of mining or extracting the rock from the ground. It is all a part of the process of extracting the metal from the ground; it is a continuous process. If the owner of the ground has no smelter to melt concentrates for him and because of the impossibility of segregating the concentrates in the smelter or refinery, sells it to a smelter and passes the title, he still only gets paid on the basis of net total content less the costs which he himself would incur if he did it himself, and the smelter thereby profits. Now that fact that the smelters may make a profit on it doesn't make any difference. *I don't think I agree with Mr. Hardy for instance, that the smelter should be allowed depletion. I think the mine owner, the fellow that has got the rock in the ground, that is having it taken out and depleting the value of his property, is the only one that can logically be allowed depletion.* The smelter, it is true, may depend for its life upon the life of the mines in the vicinity that it serves, but it should figure its depreciation and obsolescence allowances on its structures, which are the only assets it has. It does not have any mineral deposits; if it has, it should be allowed depletion on those, but it doesn't have assets as a smelter other than physical structure. *I think the depletion should all go to the mine owner whether or not he beneficiates his ore or sends it to a smelter. If you do that you have an absolutely logical position.* [Italics supplied.]

What has happened under these regulations, the Treasury says, "Oh, no; if the mine owner mines the ore and sends men down underground and digs it out, then crushes it, puts it through flotation, obtains concentrates, sells those concentrates to a smelter, he is selling a [762] first mineral product. The first mineral product is not the mineral, but the concentrates. Therefore, anything that tends to beneficiate concen-



trates is something beyond the value of his product and he should only be allowed to claim depletion on the value of the thing he receives less the cost of getting it from the mine bottom to that point." Well, they take the instance of the man who sells to the smelter and they have perhaps a little argument there. Then they come back and say, "Well, if the company itself owns a cyanide plant and refinery we have got there a theoretical computation that they are selling the concentrates to themselves after they get them through the flotation, and subtracting the cost of the cyaniding."

Then, they come to the quicksilver people and that is a very hot argument right now. It deals with a highly strategic metal and they do not have any milling or any cyaniding in the case of quicksilver. The ore produced is cinnabar. It comes out in the form of an ore containing some perhaps 6 pounds to 20 pounds of mercury to the ton. That means if it is sold in flasks of 75 pounds of metal, you would have to transport from 4 to 12 tons of ore to get one flask of metal, and that is just out of the question as an operative proposition. Well, the ore goes from the mine through a primary crusher into a rotating furnace and is roasted. The Treasury says that is just like a smelter, you roast it, therefore that cost is out. From the rotating furnace it goes into a condenser and the liquid metal itself comes out of the condenser. There is no intermediate process. Now they have not in this regulation even mentioned quicksilver; they tried to draw an analogy to other ores and say because we deduct the cost of roasting copper, lead, or zinc ores, before arriving at "gross income" therefore we are going to deduct the cost of roasting quicksilver *although it is essential, in order to get any marketable product, that this roasting be*

done at the mine. That shows where the lack of logic in their whole position leads. I am going to come to a suggested remedy in a few minutes. [Italics supplied.]

They pass from one step to another, subtracting first the cost of roasting the concentrate where they go to a smelter. They say they have been sold to the smelter or the refinery, then. If you do that you must charge the owner who has his own smelter or refinery the same if you are going to deduct the cost of roasting so as not to discriminate in favor of the big fellows. *There is no more reason for deducting the cost of cyaniding, then, because the regulations don't say anything else, than there is for a deduction of the roasting cost.* Then they come back to mercury, which is not similar, and deduct what is tantamount to the entire milling cost in getting at the gross income from the land on which depletion is to be computed. The next thing, of course, if they are logical, will be to say, after all cyaniding is a considerable part of the cost of getting the metal out, and so is milling. "Let's take the milling cost out;" and then, after they have done that they might as well say: "We will disallow the extraction expenses, mining and everything else, because that is part of the cost of getting the metal out," and then you will be allowed 15 percent, not of the gross income from your property, but of the net income. Congress says, the law passed by Congress says that you may have 15 percent of the gross up to 50 percent of the net. Logically carried out the present course of action of the Treasury leads to just that at third conclusion, and it distorts the intent of Congress and removes all of the benefits of the depletion allowance from the owners. [Italics supplied.]

[763] Now, what remedy can be found for this? I told your committee at the beginning that I did not

suggest any amendment of the sections dealing with percentage depletion. I think if you take section 23 under the act, persuade your Senate Ways and Means Committee to insert a simple definition of gross income from the land as being the gross value of the metal derived from that land, allow the owner of the land to take a 15 percent of it, limit him to 50 percent of the net, then the thing would be simple of administration and a lot of this temptation to chisel which the present regulations give would be wiped out by the act of Congress itself. I think the original intent of Congress, which was to allow the mine owner to deduct depletion for that which he was wasting and losing and operating as property would be carried out, and the Government would not lose by the operation, particularly as the additional certainty and security which this would give mine operators would tend to encourage the development of new bodies of strategic minerals which are very much desired today. Thank you, gentlemen.

The CHAIRMAN. Are there any questions?

Mr. HARDY. *I wish to make a statement to the effect that I thoroughly concur with Mr. Searl's idea of depletion on a custom plant, but I do think there are certain circumstances whereby if a custom plant is built to treat ore in a certain restricted area, a certain amount of ore, they may be entitled, the case might have some merit of depleting, but such plants always have the depreciation to fall back on anyway. [Italics supplied.]*

Mr. ANDRESEN. You spoke from time to time about the chiseling attitude of the Bureau in this matter.

Mr. SEARIS. I did not mean that in a disrespectful tone, Mr. Andresen. I used it as we commonly use it. I think you have been whittling down what was orig-

inally intended as an equitable allowance to mine operators—I call it chiseling for short.

Mr. ANDRESEN. To preface the question, I would like to outline a case to you. Basically we have the conception we should treat all taxpayers alike. I think you will agree that we have tried to do that. The act which speaks in terms of mines, oil and gas, and gas wells, timber, and other natural deposits, never speaks of smelters, manufacturing plants, marketing systems, or transportation systems. Early in the days of percentage depletion oil and gas companies took the product of the well, put it through a plant and produced gasoline, and then said to us, "There is the first marketable product." This is what Congress intended percentage depletion should apply to. The Court settled it in the case of *Signal Gasoline Corporation v. Commissioner*, 77 Fed. (2d) 728, and held that Congress intended that the percentage depletion should apply to the price at which the product would have sold at the mouth of the mine or well and not to the price for which the refined product was sold.

*In the committee hearings, it was made clear that the basis of gross income for the property was to be net smelter returns to the operator of the mine; in other words, depletion relates to the price he could get for the concentrates from a smelter, assuming that the smelter would get a reasonable profit for the investment in addition to its depreciation and costs. We then found ourselves face to face with taxpayers who own mines, smelters, refineries, and marketing systems. These [764] taxpayers contended they should have depletion based on the sale of the refined product—the metal. If we had allowed that, it would have provided them with a substantially greater depletion allowance than the miner would*

have, who only owns a mine and a mill. That matter has been pending before the United States Board of Tax Appeals for some years now. In a comparative situation taxpayers who owned producing properties, pipe lines, transportation systems, and distribution systems in a city contended that the only marketable product produced was the gas sold to the consumer and used in the house, and that the Congress intended that the percentage depletion should apply to the ultimate selling price of the product. The United States courts decided two cases holding that the percentage depletion would have to be computed on the price for which they would have sold the gas at the well (*Consumers Natural Gas Co. v. Com.*, 78 Fed. (2d) 161; *Greensboro Gas Co. v. Com.*, 79 Fed. (2d) 701). *What the mine owner would have sold the ore\* for in the form of a concentrate at the mine provides the gross income from the mining property for percentage depletion purposes. When he beneficiates the product in greater degree, we must deduct from the selling price the costs of other processes such as smelting, roasting, refining, selling, and the proportionate profits attributable to those, to arrive at gross income from the mining property. Don't you think that this is basically fair to taxpayers and puts them all on the same basis? [Italics supplied.]*

Mr. SEARLS. No, sir; I do not for this reason: In the case of oil and gas wells you have produced a product which is marketable, a product with many uses and many possibilities as it comes out of the well, also there is a field price for crude oil dependent on market—a field price for gas if there is any market for it at all. There you have an ultimate product upon which refining operates to reduce it into further constituent elements which may be the gasoline, hydrocarbons, various grades of kerosene distillage,



fuel oil, finally winding up in asphalt. *Obviously it was not the intent of Congress that those processes which would take your products and make them into different products having very different uses should be considered, as the basis of depletion.* But I say in respect to metals that that is not true because the thing that comes out of the mine in the first place is just ore; 90 percent of it is waste unless it is high grade, and it has not any market value at all. That certainly is true in the quicksilver case, the quicksilver mines are before your committee now, and it is equally true of practically all mines. Maybe a few high grade gold ores could be sold and stand the cost of transportation, but very few. Now you come to concentrates; it is the same thing. It is true that a man may employ a smelter to do the concentrating, he may even transfer title of the concentrates to the smelter. What you get out of it is not a market price for the concentrates. He gets the value of the metal less the cost of treating concentrates, and it is a very different situation than the oil wells, and I don't think that the cases which you mention, with which I am very familiar, have any proper bearing on the situation when it comes to distinguishing between the mine owner who owns his own mill, refinery, smelter or cyanide plant, and the fellow who doesn't own it. I see no reason for giving the big fellow that has all those big works any better or any worse deal than the little fellow who hasn't got them. I say that the refining process has nothing to do with the depletion. [Italics supplied.]

[765] Mr. ANDRESEN. To test out your theory, I know of an actual case. I will not name the taxpayer. This taxpayer owns a mine, owns a railroad, a large smelter, and an electric refinery and a shipping and marketing system which sells copper all

over the world on a world market. In that case an attempt was made to compute the gross income from the property reducing the selling price of the metal by the cost of the selling, or marketing, the cost of refining, the cost of smelting, the cost of railroad transportation.

Mr. SEARLS. That was to comply with your regulation, wasn't it?

Mr. ANDRESEN. No; it was not. It had the effect of putting all of the profit in the mine.

Mr. SEARLS. Yes; I think—

Mr. ANDRESEN. Do you think it belongs there? Why would people build smelters if all of the profit is in mining?

Mr. SEARLS. A man who owns the mine doesn't want to build a smelter, so he gives some of his profit to somebody else. That is all right.

Mr. ANDRESEN. If he does, why should a manufacturing company or a smelting and refining company be entitled to depletion when its full investment can be recovered from depreciation?

Mr. SEARLS. It should not, *but it should be allowed depletion on the metal value in properties from which metal is mined without subtraction for the cost of concentration on the theory that a gross return from the property is the value of the metal in it. It is not its "gross income," but it is "gross income through the property."* [Italics supplied.]

Mr. ANDRESEN. One more question. Take two identical mining properties, in one instance in which the miner produces a concentrate, and in the other instance builds a smelter and goes all the way through refining to the metal. Wouldn't your proposal give substantially more depletion to the one who manufactures the finished product?

Mr. SEARLES. No.

**Mr. ANDRESEN.** Fifteen percent of a greatly augmented selling price?

**Mr. SEARLS.** No, sir; in a gold operation the price of the metal is \$35 an ounce, fixed by law. No producer would get \$35 an ounce for the metal if he shipped the concentrates extracted to a refinery.

**Mr. ANDRESEN.** That makes a substantial difference.

**Mr. SEARLS.** I cannot see that; if he elects to invest his capital in the erection of the refinery, well and good, but the thing that is of value in the refined product is the metal and the ultimate value of that metal is the thing I think on which Congress intended depletion to be computed. If it is computed on that value, all your troubles are going to disappear.

**Mr. CAMPBELL.** This is a technical question we are on. In all probability it is a subject which will be adjudicated by the courts. I should like to ask Mr. Searls, if I may, what bearing that has on the curtailment of production. Can he cite cases in which this situation is held up the efforts of the War Production Board in trying to get metal output?

**Mr. SEARLS.** I cited two cases, one dealing with chrome, the other with copper operations, both of which are strategic metals in which the attitude of the Treasury on depletion as well as the excess profits tax were sufficiently determined to prevent further production. I [766] cannot separate the exact weight of the two upon the proposed investors, but they are both operating.

**Mr. CAMPBELL.** Was the question of depletion you are discussing now, the attitude regarding the allowance of percentage depletion?

**Mr. SEARLS.** The Treasury interpretation on the depletion act. I don't think that the taxpayers would have been bothered by 15 percent of the gross at all if the gross had not been whittled down to a point

where it is going to be negligible. To illustrate that, suppose a man had a property on which he sold the concentrates and made a profit, say, of 50 percent on the gross, and then the Treasury comes back and deducts a lot of these things and allocates a proportion of his profit to each of the corporations which he used in getting these concentrates, equal to the profit he made on the whole operation. Eventually he would wind up with practically no income at all because if he made a large profit and the Treasury insisted on apportioning each of these operations which it subtracts from the gross income, by the time you have done that, theoretical profits on milling, cyaniding, and other things added to the actual cost, you will find practically all of your gross income is used up in deductions for theoretical profits. Now, by my mind it is ridiculous.

The CHAIRMAN. Gentlemen, we thank you both for the colloquy. I think it was enlightening. While getting the enlightenment we are being entertained as well.

[812]

Statement of Alex F. Ross, Mining Engineer, Superintendent of the Argonaut Mining Co., Jackson, Calif.:

Mr. Ross. My name is Alex F. Ross, superintendent of the Argonaut Mining Co., of Jackson, Calif. As my good friend McBoyle said yesterday, I am not a taxation expert, although I have done a lot of hard-rock mining, and I call myself a soft-ground miner. [813] At the Argonaut we were producing 8,000 tons of ore; our explosives cost less than \$1,000, but our timber cost between four and five thousand dollars, which is an aside to show the character of our work.

When I got notice of this meeting I was told by the secretary of our company I had better come up here. Jackson is only 140 miles away from here.

This word, "beneficiation," kind of stuck in my craw. I can understand how a coal mine can bring coal out of the ground, take out the slate and the wood and other things like that, and crush it and grade it so that it can be used for domestic purposes. I can see where beneficiation can apply to that. I can also see where beneficiation could apply to taking iron out of a mine where some waste materials are probably in that iron ore and what you are after is that iron, just like in a coal mine, what you are after is the coal, but when it comes to these strategic metals, and although I may differ with some of these, they find strategic metals, I think gold is the most strategic metal of all. Sooner or later this war has to be paid for and it has got to be paid for by gold. *I was very glad to hear Mr. Searls' remarks yesterday. If I had written his brief for him, whether I could or not, I doubt whether I would have said anything different from what he said. In other words, he said exactly what I feel about this whole thing.* There is no such a thing as beneficiation in gold ores. That will apply to strategic ores, too. *What we are after is the mineral in those ores.* Now, for the sake of argument if we can bring ore out of our shaft that goes \$10 a ton at the door at the shaft, after we get through our different processes it is only worth \$9.40, all we can make is a 94-percent ratio. Now, we have a ball mill and cyanidation process for taking out the gold because we have considerable free gold in our ore, high-grade sulphates; *now then, when you fix the cyanidation as being something entirely different from these other things, it seems to me you are putting the wagon in front of the donkey.* Cyanidation is something that came into use in the second



decade of the century, flotation was practically not used until the third, and fourth, and it is only lately, before this war started, that flotation has become a part of our metallurgical processes. *When you are picking out cyanidation to find a flaw with, I don't see why you can't go back and pick out flotation, and finally our ball mill, and also, if you want to, the rock crusher.* The thing leads from naught into absurdity. There is such a thing as beneficiation for ores within coal and iron and things where you are going to sell the product that comes out of the ground, and are doing something to make that produce more valuable. In the gold and other strategic metals what you are after is the mineral in the ore, and the ore, when you get the mineral out of it, you put out in a dump pile and tailing pile or some place like that. [Italics supplied.]

Just in closing, gold mining has so many quirks that no new ones should be added. Even *this cyanidation item* would only make a little bit of difference to some of our gold miners; you know, gold has its value set by the Government and all of the increased costs put on gold mining cannot be passed on to a consumer, and to a large extent that is also true of our silver mining where silver is set by Government price. Those are the things you want to remember. There is no such thing as beneficiation of gold ores, and most of the strategic mineral [814] ores in the sense that you can improve the product after it comes out of the ground and make it more valuable. All you can do to it is to make it less. There is also a tailing loss on every operation. Thank you. [Italics supplied.]

Statement of S. H. Williston, President, Oregon Mining Association:

MR. WILLISTON. Senator McCarran, Senator Murdock, and Governor Maw: Though I was at the Reno hearing I did not hear the first part of your Reno meeting. I gave one or two examples there which were, I believe, pertinent. Since then there is another example which is quite pertinent to this inquiry.

This example has to do with the depletion allowance. In the bill the depletion allowance provides for a 15 percent of the gross not to exceed 50 percent of the net of the gross proceeds from the mining property. *A miner understands that as what he gets for his product. The Treasury Department does not necessarily understand it the same way. They have made a ruling which has this effect, not upon copper, or lead or zinc, but it has this effect upon gold or mercury, tungsten, and probably on chromium. The Treasury's ruling, as I understand it, and I hope I am right, I may be wrong, is that if the ore is benefited that the character of the ore is not changed, then the gross proceeds from that concentrate is the basis for the depletion allowance. If, on the other hand, the chemical conditions of that ore have changed, then that process, the cost and the profit assigned to it, must be deducted, and the gross receipts may be much less. Now, it is that particular point on which I would like to give some examples from the quicksilver industry which are applicable in a way to gold, and, I think, are quite applicable to some tungsten properties, and possibly to the chrome. [Italics supplied.]*

In the recovery of quicksilver the ore ordinarily is crushed and goes into a furnace. In the furnace it is changed from mercury sulfide through oxidation to mercury vapor and sulfur dioxide. It does not

come under the Treasury's ruling. Consequently the basis for depletion in a mercury mine is the ore at the crusher. Now, the ore at the crusher could not be given away. Without going through the furnace the value is far less than the freight on it to the nearest railroad. Now, it so happens that it would be perfectly feasible to use a flotation scheme instead of furnacing, and flotation would probably be about 5 percent less efficient because there would be a double loss, first, from the flotation and, second, from the retorting of the concentrate, but it has not been done in the past that way, and the net result is that the quicksilver mines, instead of getting a 15 percent [859] depletion rate, gets depending on the relative cost of the mining and milling, a 5 percent depletion, a  $7\frac{1}{2}$  percent depletion, or a 10 percent depletion and possibly in some cases a  $12\frac{1}{2}$  percent depletion. In a case where it is an underground mine and the cost of mining, we will say, is 2 to the cost of furnacing, which is 1, then the depletion rate would roughly approximate 10 percent because there are 2 parts in the expenses in mining, 1 part is in furnacing. In other words, the high cost underground mine gets its higher rate. If, on the other hand, it should be an open-pit proposition, where the mining expenses are low and the furnacing costs in comparison are high, the ratio might easily be 3 to 1. In the other connection then, one-fourth of the 15 percent, or about 4 percent, would be the basis for depletion, and 12 percent would not be allowed. Now, when the ruling of the Treasury was passed, I think this dates back a good many years, quicksilver was not considered to be valuable, nobody paid any attention to it. The industry was so small that it did not make any difference. It has only been, as I understand it, within the last few years that this has been progressively applied

to the quicksilver industry. Now, that effect on the quicksilver industry might be overcome by an appeal for special provisions or some such thing to the Treasury Department. However, all of the quicksilver companies are small, comparatively, and they cannot, the individual corporations, justify their existence by the expense of the lawsuit. In other words, it is better to pay "through the nose" or it has been in the past.

Now, that depletion basis is almost the only basis on which a mine can recover its investment. Returned profits are more or less ruled out, so if you cannot recover your investment on the depletion basis you cannot get it. If, instead of the 15 percent which most miners expect, we get 4 percent which as lawyers we are allowed, we cannot do much with it.

Now, the effect of that on gold is probably understood fairly well. If you use a flotation system or if you use gravitational methods then the gross value of your product is the base for your depletion. If, on the other hand, you use cyanide you change the character of the gold, you dissolve it and you get it out in a different form, and the cost of that is not permitted.

Insofar as tungsten is concerned, I believe some of the tungsten properties in Nevada are starting with scheelite, dissolving it and making artificial scheelite in a third process. They have changed it and wound up with a product which is practically the same, but not exactly the same. If the Treasury Department should take that literally, then all tungsten beneficiation of that type would not be allowed and a tungsten mine would deplete not on a 15 percent basis but on a 5 percent which is a comparatively expensive process.

If you jump to chrome, there again the Treasury regulations say flotation or gravitational methods some of the new chrome plants in Oregon are using or expect to use, electrostatic separation of the chrome beach sands, that is not included, but since the chemical change is not made there it would probably get by. If, on the other hand, they pursue the process and put in a roasting plan with  $\text{SO}_2$  to change the chrome iron ratio they will be penalized for bringing up the grade by losing a portion of depletion allowance.

[860] The two examples I have in mind are two mercury properties, one in Nevada and one in Oregon. One is an underground mine. The ratio of costs of the two is about \$2 mining versus \$1 for furnacing. That mercury mine under the present plan could be entitled to approximately a 10 percent depletion basis percentage. The Nevada property, on the other hand, has a relation of probably 3 to 1 in the other way. The expense is largely of furnacing and very slight expense is in the mining. It is going to be reduced to a 3 percent depletion base. That particular property, as it so happens, was started the year that the Senate gave the strategic metals exemption from excess-profits taxation. It was completed in a year in which we got taxed and it is just tuned up and going in a year in which it will get the trousers kicked out of it. It will not last out an appreciable amount of time, probably 1 year. In Reno I was considering that a 15 percent depletion might possibly let that property break even. If it is only to get a 5 percent depletion it cannot possibly break even because it has no previous earnings, and an investment of \$200,000 which might give back \$8,000. The 10 percent of the excess profits would be very small, and the 5 percent depletion even on half a million dollars gross would not come anywhere close to being of any help.



Senator MURDOCK. May I ask this question: Would it be a fair construction of your statement to say notwithstanding the fact that the Congress intended to give mines a percentage depletion of 15 percent under the rules and regulations promulgated by the Treasury that is cut down to as low as 5 percent?

Mr. WILLISTON. I can see how it might be. That is the way I understand it. If I am wrong I would be only too glad to hear it.

Senator MURDOCK. I think you know much more about it than I do. I think that would be a fair conception of your statement.

Mr. WILLISTON. That is exactly what I say. It is possible to get it down, not possibly as low as three, but certainly as low as five. It is bedded on the technicality. *There are reasons in certain instances for making provisions like that. You might take, for instance, a copper mine, or an iron mine, it would be better to take an iron, for instance, where you mine the ore, you haul it to the smelter, you turn it into pig iron, haul it so much, you turn it into steel, and you base depletion for the mine on the value of the steel rolled into finished shapes.* [Italics supplied.]

SENATOR MURDOCK. *Would you consider that a fair construction of the 15 percent depletion?* [Italics supplied.]

Mr. WILLISTON. No; that is the basis, I understand, that the Treasury did not like to grant it on and started from there back, made an artificial cost, or ruling if the character of the ore has changed then we cannot allow anything. Maybe it is applicable in an iron mine, I am not familiar with the iron business, but when it comes to a process of recovery of the metal which is located at the mine and which you cannot sell as the product I think the ruling is somewhat arbitrary and certainly it is going to have

a disastrous effect on any operation which is governed by that ruling. You might say that now, before you put in a quicksilver plant, you should consult with your attorney whether the plant should have flotation or furnacing, because it is really up to the attorney's decision and not the metallurgist as to which one to follow. [Italics supplied.]

[861] Senator MURDOCK. The attorney might be wrong, too, and ruled out by the tax collector.

Mr. WILLISTON. Well, it is out of hand for the metallurgist. In other words, it requires a technical decision as a tax expert and not a metallurgical decision.

SENATOR MURDOCK. *Now, take the Utah Copper out here which produces a low-grade ore. I doubt that their ores are salable to anyone after it is mined, but it must go on through the concentration process before they would have anything to sell. Isn't that true?* [Italics supplied.]

Mr. WILLISTON. *That is true, and inasmuch as it is flotation that, according to the Treasury rules, is permissible, but if they had a chemical process then I doubt if it would be permissible.* In other words, if it comes out as a chemical precipitate of pure copper I don't see how the Treasury could allow that, if the ruling is the same that it is on quicksilver. It is a ruling for the Treasury, though, I think the Treasury does not like to be forced to make that ruling. They have to draw a line somewhere, I suppose, so they have to do it. I know the miners would be much more pleased if the Senate would make the decision and make it hard and fast and we could make it hard and fast and take the load off the Treasury Department. I hope they would appreciate it. I would like to save them work if we could, but that ruling as it is, especially on the new strategic metals not consid-

ered in the past, which were not produced in the past and which are being handled by entirely new and different processes are going to suffer tremendously on that account. Any chemical change in the ore value cannot be permitted in that base depletion but it has to be taken out as a cost, the profit applied to that particular process, and also has to be taken out. It is not as if you could take off the cost of that, but if the cost is half and half and they disallow processing then half of the profit is applicable to that and cannot be used as a depletion base. It is a point which I did not bring up at Reno because I had heard about it later. I thought it was important to get it into the record here. [Italics supplied.]

Senator MURPOCK. Did you hear Mr. Searls, the attorney from San Francisco? I think he suggested an amendment, did he not?

Mr. CAMPBELL. To take care of the situation we are now discussing?

The CHAIRMAN. Thank you very much, Mr. Williston.

Mr. CALLAHAN. In connection with that interpretation and this ruling by the Treasury, with regard to change of the character of ore due to a chemical process, I happened to be present before the Finance Committee when the original percentage depletion amendment was put in the law, and following that I was present at conference held with the Treasury officials who were going to write the regulations. I can say definitely from my own memory as far as those conversations at that time, in writing the regulations for the amendment which had just been passed by the Congress, I know very definitely there was no intent other than the 15 percent depletion allowance would apply in a case such as Mr. Williston refers to.

Mr. WILLISTON. I am glad to hear that, Mr. Calla-

han. One of our quicksilver companies has a tax appeal up now. The Treasury feels the other way about it, and it has gone to the appeal court, but the Idaho Alma Dean has to deduct it. That is Idaho's former largest producer. The Bradley Mining Co. and Gould in California both have to suffer under it, they have a deduction on that account, and [862] the Bonanza Mining Co. have all, I believe, a tax-appeal case up. I think they are the first ones to fight it, but I know it has been brought to the mercury industry within the last 3 years.

Mr. ANDRESEN. May I make a statement?

The CHAIRMAN. Yes, Mr. Andresen.

Mr. ANDRESEN. In connection with this matter, the phrase "ruling" has been used rather frequently. To clear the record, I would like to point out that the provision referred to is not a ruling of the Treasury, it is the provision of the regulations which were promulgated by the Commissioner in 1932 to give effect to the Revenue Act of 1932 and which was amended in the regulations promulgated in 1940. Regulations 103 provide:

(f) "Gross income from the property," as used in section 114(b) (3) and (4) and sections 19.23(m)-1 to 19.23(m)-28, inclusive, means *the amount for which the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine or well, but, if the product is transported or processed (other than by the processes excepted below) before sale, it means the representative market or field price (as of the date of sale) of crude mineral product of like kind and grade before such transportation or processing. If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting*

*from any process or processes (or, if the product in its crude state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation and the processes not listed below). The processes excepted are as follows:*

(1) In the case of coal—cleaning, breaking, sizing, and loading at the mine for shipment;

(2) In the case of sulphur—pumping to vats, cooling, breaking, and loading at the mine for shipment;

(3) In the case of iron ore and ores which are customarily sold in the form of the crude mineral product—sorting or concentrating to bring to shipping grade, and loading at the mine for shipment; and

(4) *In the case of lead, zinc, copper, gold, or silver ores and ores which are not customarily sold in the form of the crude mineral product—crushing, concentrating (by gravity or flotation), and other processes to the extent to which they do not beneficiate the product in greater degree (in relation to the crude mineral product on the one hand and the refined product on the other) than crushing and concentrating (by gravity or flotation).*

In case any of the accepted processes are not applied in the immediate vicinity of the mining district in which the mine is located, costs incurred for transportation to the processing location and, if transported by taxpayer, the proportionate profits attributable to transportation should be subtracted from the sale price of the product to determine “gross income from the property.” [Italics ours.]

This general question involved here has been the subject of litigation in connection with the oil and gas cases for a number of years. The Supreme Court of the United States in the case of *Wilshire Oil Co.*, 308 U.S. 90, declared that this phrase “gross income from the property” and “net income from the prop-



erty" as used in these regulations from which I have quoted is an ambiguous phrase peculiarly appropriate for administrative construction and interpretation and denied the contention of the Wilshire Oil Co. in that instance as against the ordinary interpretation of these words. The Court held for the Government on the ground that the provision was an ambiguous phrase and the Commissioner's interpretation of it was reasonable and fair.

We have had, admittedly, a difficult problem in the administration of this law. It has been in my experience in the past 18 years in the Bureau of Internal Revenue that this is one of the most difficult problems. I have been repeatedly accused by taxpayers of being hard- [863] boiled and unsympathetic with their problems. On the other hand, the Treasury is today face to face with a number of very important cases involving large sums of money. In one of them the Commissioner is the defendant in a suit for a refund for very large sums which involve the basic question we are considering here. So you can see, perhaps, from my remarks, this is not an easy question, and I hope I have convinced you that I have no desire to be anything but sympathetic for the mining industry in this matter, no desire to do anything but administer this law in a way that produces a fair and equitable result.

Mr. CALLAHAN. May I say when I stated I had conversations with the Treasury following the passage of this law, I realize Mr. Andresen is correct regarding the regulations of the Bureau of Internal Revenue. One remark I would like to make is that where there is such an ambiguity, it seems strange that inevitably the Bureau of Internal Revenue and the Treasury find it much more convenient to determine and resolve that ambiguity against the taxpayer.

Now, sometimes we would like to have just a little bit more sympathy, and we would like to have it understood that the taxpayer is the one, after all, for whom these tax bills are written. *In this particular case there is no question about the understanding about that percentage depletion amendment or why it was written into the law. It was to apply that way. An ambiguity crept in there as a matter of language. It is just too bad, of course, and it is also too bad that the questions ever have to come up. [Italics supplied.]*

Senator MURDOCK. May I ask you this question, Mr. Callahan: At the meeting at Reno we seemed to have a difference of opinion there between two people speaking for the mining industry, one a mining engineer, as I recall it, and the other an attorney for large mining interests. *The mining engineer, as I understood him, wanted to include the smelting charges, add them in connection with your gross, whereas the attorney of the mining interests seemed to think that was going a step too far. Have you got anything to say on just where the process on crude oil and, say, the copper, the lead, or the zinc in the metals state; should this rule be applied in regulations? [Italics supplied.]*

Mr. CALLAHAN. *Of course, a mining engineer, being an operator and interested in the product would want to apply the smelting charges as well, but I am a lawyer, so I have to take another viewpoint. I don't think that was ever intended in the law. I don't think it was discussed. I will have to take the lawyer's viewpoint on that. [Italics supplied.]*

Mr. FERNALD. Mr. Andresen is referring to the first regulations. I would like very much if he would read in the phrase as to what it was that was to be excluded as to processes beyond those referred to, the phrase

which, in those regulations, was, after considerable consideration by the Treasury, written as the cost of those processes, and *it was only some years afterward that "profits attributable thereto" was written.* In the first one it was confined to cost of the substitute process, not attributing any profits to them. I think Mr. Andresen has that phrase before him. [Italics supplied.]

MR. ANDRESEN. Mr. Fernald has described the situation. The regulations of 1932 provided that:

\* \* \* in the event it was necessary to work back from the price of the refined product to get the gross income at the mine, it was to be done by deducting the [864] cost of the processes which came after crushing and concentration, by gravity, or flotation.

The provision of the regulation is written that way. The Commissioner found that a substantial number of taxpayers were making the computation in that literal way, and that it had the effect of putting all of the profits from marketing, refining, smelting, and rail-roading back into the mine. In other words, we almost concluded that some of the great copper mines of the world were actually gold mines because all of the profits that were derived after the ore passed out of the mine were ploughed back into the mine in their computations of the depletion allowance. Therefore the Commissioner amended the regulations. Treasury Decision 4960 promulgated in January 1940 introduced into this paragraph a phrase:

\* \* \* requiring the deduction of the costs of these additional processes and the proportionate profits relating thereto.

*The amended regulation had the effect of giving all taxpayers the same basis for a depletion allowance, namely, the actual gross income from the mine alone.*

*The treatment contended for by Mr. Fernald and others would greatly favor the major operators who own and operate smelters and other facilities in addition to mines. [Italics supplied.]*

This Treasury decision has now been in force for some 2½ years. Since then the Congress has enacted the Revenue Act of 1940, the Second Revenue Act of 1940, the Revenue Act of 1941. Under the rule that the successive reenactment of the statute after the regulation has been changed the Commissioner would contend that the regulation now has the force and effect of the law.

Mr. FERNALD. Might I observe the contemporaneous interpretation of the law at the time it was first passed in 1932 was that the word "profit" should not be included? Mr. Andresen's statement is that that continued while we had the Revenue Acts of 1933, 1934, 1935, 1936, 1937, 1938, and 1939 so consequently that must have been the law in 1940, isn't that clear?

I would also like to bring out that for those many years it was customary to deal with the matter of the cyaniding, if I am rightly informed, under the Treasury regulations, so as not to exclude the entire cost of the cyaniding process, but only so much of that as was considered as going beyond what a concentrating cost would have been, and it is only very recently that the new rulings or interpretation which had existed for 8 years, since the early interpretation of that section. I think I would be very much interested if Mr. Andresen will state for the record just what was the early interpretation of the cyaniding proposition.

The CHAIRMAN. Would you care to state that, Mr. Andresen?

Mr. ANDRESEN. I think Mr. Fernald has given us a correct picture of the early interpretation of the original regulation. After some years the Commis-

sioner came to the conclusion it was producing a result that was not in keeping with the intent of the Congress in this matter, hence the regulation was changed in 1940.

[999]

Statement of HENRY B. FERNALD, Chairman, Tax Committee, American Mining Congress:

[1001]

#### TAXATION

[1002]

In addition to the foregoing, there has been criticism expressed of certain rulings and interpretations by the Bureau of Internal Revenue or its employees; particularly as to its interpretations and practice regarding "gross income from the property" in computing percentage depletion. As hearing on this matter, I am filing a memorandum, exhibit A, which brings out (1) the meaning this term was intended to have as used in the first report of the staff of the joint congressional committee regarding percentage depletion of mines, and (2) certain recent changes in Treasury interpretation or Bureau practice. This memorandum may be helpful in the further consideration of this subject.

[1008]



## As to the Meaning of "Gross Income From the Property" in Computation of Percentage Depletion

*Criticism has been voiced of the present Bureau practice in determination of the allowance for depletion to represent 15 percent of the "gross income from the property." This is not the time nor place to argue whether or not the Bureau practice gives the proper interpretation to the wording of existing law. The basic thought here expressed is that such interpretation does not give to many mines the allowance which they should have and which they thought was granted them when the law was enacted. It does not even give to many the allowance which the Treasury Department, by its regulations and administrative practice, granted to them for many years after first enactment of this provision. [Italics supplied.]*

(1) As to the original intention of this provision, reference is made to a report of Alex R. Shepherd to L. H. Parker, Chief, Division of Investigation, Joint Committee on Internal Revenue Taxation, which appears as Appendix XXXI, page 65, to a report of Mr. Parker to Chairman Hawley, September 17, 1929, and of Chairman Hawley to the joint committee, September 19, 1929. (Reports to the Joint Committee on Internal Revenue Taxation From Its Staff, Vol. 11, p. 8, 1929.) [Italics supplied.]

[1009] In that report (p. 67) it is stated—

The average depletion allowed for all metals is approximately 17 percent of the gross sales for this period.

Also on page 67 is—

Table 1.—Summary of the metal industries for a 5-year period (1922-26), showing the gross sales (equivalent to the gross income from the property) \* \* \*

On page 68 it is stated—

Table 1 shows that the metal-mining industry has received in depletion allowances an average deduction equivalent to about 17 percent of the gross sales.

From the study of this subject it is believed that 15 percent of the gross sales value with a 50 percent limitation to net income, would be a reasonable rate to allow the metal-mining industry for the future. This reduction by 2 percent of the actual figures shown in the summary is thought advisable to offset the continuing effect of the percentage-depletion method.

Elsewhere reference is made to—

- 15 percent depletion allowances on gross sales;
- 15 percent of their gross sales;
- 15 percent to gross sales.

Thereafter, on page 70, the report recommends that the wording of the act should follow that for oil and gas, reading "15 percent of gross income from the property," and that the necessary definitions should be written into the regulations.

On pages 72-73 there is a discussion of various metals and the basis to be used, with the recommendation that—

For the purpose of this subdivision "the gross income from the property" shall be the competitive market receipts, or its equivalent, received from the sale of the crude, partially beneficiated or refined gold, silver, or copper, the product actually disposed of by the taxpayers to govern the method of computation of receipts in all cases, and in the case of all other metals, coal and oil and gas, the competitive market receipts, or its equivalent, received from the sale of the crude products, or concentrates on an f.o.b. mine, mill, or well basis.

Illustrative examples are given (pp. 74-75) showing the results of the 15 percent computation:

For lead, 15 percent of a 7.53-cent sale price per pound of lead;

For zinc concentrates, 15 percent of a \$50 per ton gross/sales price at mill for the concentrates;

For iron ore, 15 percent of a \$2.68 per ton sales price f.o.b. cars at mine for the ore;

For copper, 15 percent of a 14-cent sales price per pound of copper.

There can be no question that this report contemplated that the 15 percent "gross income from the property" was to be applied to the finished metals recovered where that was the established form in which the product was marketed. This was clearly the contemplation as to copper, lead, gold, and silver. (No thought seems to have been given at that time to such products as quicksilver, which were not then important subjects of domestic production, but the furnacing or retorting of quicksilver ores is generally regarded as the equivalent of concentration.)

Without argument as to the legal weight which should be attached to this report, we may at least say it gave substantial support to the belief that this was the interpretation which should be placed upon the expression "gross income from the property."

(2) *As to the Treasury interpretation, the original regulations prescribed that for "lead, zinc, copper, gold, or silver ores and ores [1010] which are not customarily sold in the form of the crude mineral product" a cut-off should be made at "concentrating (by gravity or flotation) and other processes to the extent to which they do not beneficiate the product to a greater degree \* \* \*," and "the costs" of any further processes or transportation were to be deducted from the sales price to arrive at a "gross income from the*

*property."* Under this regulation, if a company sold its own metals, the costs of smelting, refining, and transportation (beyond the concentrating stage) would be deducted from selling price realized, and the remainder would be "gross income from the property." [Italics supplied.]

Moreover, under this regulation, the Bureau in practice considered cyaniding as substantially equivalent to concentrating, and its cost was not deducted in computing "gross income from the property." [Italics supplied.]

These regulations and this practice continued for many years (while the law was repeatedly reenacted), but in 1940 the regulations were amended to require that not merely "the costs" but also the "proportionate profits attributable to" the processes or transportation beyond concentration should be deducted in computing "gross income from the property." [Italics supplied.]

Later, also, the Bureau, with no change in law or regulations with regard thereto, has changed its practice as to treatment of cyaniding and now proposes to hold that cyaniding shall no longer be considered as substantially equivalent to concentrating; but that cost of cyaniding (plus profits attributable thereto) shall be deducted in computing "gross income from the property." [Italics supplied.]

The principal criticisms which have been presented to your committee seem to fall under the following heads: [Italics supplied.]

(a) That practice and rulings with respect to cyaniding, established when the law was first enacted and continued for many years, have now been reversed.

(b) That the regulations, as originally promulgated and continued for many years, have been changed to require or permit profits to be

attributed to certain processes and deducted in computing "gross income from the property," whereas the most that should be done, even under the original regulations, would be to deduct the costs of such processes.

(c) That the interpretation given to the law by the Regulations (whether or not legally correct) fails to carry out the original intent of the percentage depletion provision, and does not give the appropriate allowance for quicksilver and other metals.

In presenting this subject to your committee, it is not our purpose to ask you to pass upon the correctness of legal or technical interpretations of the present wording of the law; but we call to your attention the apparent need for writing into the law such definition of "gross income from the property" as will insure that the intended reasonable allowance for percentage depletion will be made in such cases.

The CHAIRMAN. Thank you, Mr. Fernald.

[1018]

(Senator McNary submitted for the record a copy of a resolution adopted by the Oregon Mining Association on August 3, 1942, entitled "Prospecting and Development of Strategic Metals.")

*"Resolved.* That our Oregon Senators and Representatives be urged to make every effort to amend the 1942 revenue bill to make it possible for private capital to explore, develop, and produce the short-lived deposits of strategic and critical minerals and metals by:

"1. Removing the excess-profits tax from strategic metals production or guaranteeing the return of capital invested in strategic metal production.



"2. Maintain present depletion allowances and make the bill more definite so that the Treasury Department may not by arbitrary regulation reduce depletion allowances as it already has with quicksilver, and may with other strategic metals.

[1037]

77th Congress  
2d Session

SENATE

Report  
No. 1582

RECOMMENDATIONS OF SENATE SPECIAL SILVER COMMITTEE WITH RESPECT TO TAXATION OF MINES ENGAGED IN THE PRODUCTION OF NONFERROUS METALS FOR USE IN THE WAR EFFORT

August 20, 1942.—Ordered To Be Printed

Mr. THOMAS of Oklahoma, from the Special Silver Committee, submitted the following:

PARTIAL REPORT

[Pursuant to S. Res. 187, 74th Cong., as amended by S. Res. 261]

[1038]

This committee makes the following recommendations with regard to taxes, based on the information which was furnished at the hearings:

(1) There must be adequate allowance for depletion. The provisions of the pending bill (H.R. 7378) should be retained. There should be no curtailment of these allowances such as proposed by the Secretary of the Treasury.

Further, the inequities created under previous tax laws and their administration, whereby mining tax-

payers have been denied the right to use the percentage depletion method through technicalities or lack of adequate notification, should be corrected for the years 1932 to 1941, inclusive.

[1039]

(11) Rulings and interpretations of the Treasury should not be so drawn as to curtail the rights of taxpayers under the revenue laws as enacted by the Congress. We criticize particularly the interpretations by the Bureau of Internal Revenue of the "gross income from the property" upon which percentage depletion allowances are computed.

**Senate Hearings, 1942**

(Revenue Act of 1942, Hearings before the Committee on Finance, United States Senate, 77th Cong, 2d Sess., on H.R. 7378)

[Vol. 1]

[969] Statement of HENRY B. FERNALD, Montclair, N.J., chairman, Tax Committee, American Mining Congress:

[970] *In the recent hearings of the Senate Silver Committee*, presided over by Senator McCarran, in Nevada, Utah, and Colorado, the representatives of the mining industry of those States and the neighboring States, such as Montana, Idaho, Oregon, California, Arizona, and [971] New Mexico, discussed the effect of taxation upon their operations. I attended these hearings and listened to the presentations made. I cannot forecast the report the committee will make with regard to them, but I state by own conclusions, concurred in by the tax committee

of the American Mining Congress. [Italics supplied.]

There was general agreement among mining men that taxation was obstructing production—particularly where additional financing was needed. To indicate why this is so, I set forth certain typical situations:

\* \* \* \* \*

[973] I. Depletion.

It is essential that proper depletion allowances be made. I shall not speak at length on this because it will be a subject of special presentation to your committee by others, but we urge that the provisions of the House bill as they are before you be continued. These fairly and rightly meet the general needs of the mining industry. There are certain special situations of which I shall later speak.

\* \* \* \* \*

[Vol. 2]

[1311] Statement of Hon. THOMAS P. GORE, Oklahoma City, Okla., representing Mid-Continent Oil & Gas Association and Independent Petroleum Association of America:

\* \* \* \* \*

[1322] Mr. Chairman, I would like to reserve the right to submit a supplemental statement in further answer to Senator Barkley's question, giving an historic background to the schedule of percentage allowances. These percentages were not fixed ad capitandum. They were the result of several investigations, both official and unofficial. One of the investigations indicated that the discovery depletion allowance on behalf of metals in a period of 5 years amounted to a little more than 17 percent of the *smelter return, which was the gross selling price of the ore*. But when Congress substituted percentage depletion, in the case of mines, it fixed the percentage

at 15, which time has proved was too little. Fortunately the percentage allowance on behalf of oil and gas was neither too little nor too late. [Italics supplied.]

(The supplemental statement referred to is as follows:)

Supplemental statement of Hon. THOMAS P. GORE,  
Oklahoma City, Okla.

[1323] The percentage depletion provisions as applied to the mining industry were not adopted by Congress until 1932. Until that time, this industry had continued to receive allowances for depletion based upon discovery value, however, the administration of same had progressively become more and more difficult and costly. It was due to these great administrative difficulties that the committees of Congress in 1932 eliminated the discovery depletion allowance in favor of a percentage of income provision.

The percentage rate was determined by studying the average of the depletion allowed under the discovery value method, taking the weighted average over a 5-year period; and it was found that in the case of metal mines this amounted to slightly in excess of 17 percent of the smelter return, which was the gross selling price of the ore.

The rate of 15 percent, which was acceptable to the metal-mining industry, was agreed upon by the Congress more or less as a compromise, and was considered conservative in view of the fact that it was considerably less than the average rate that was allowed over the prior years.

Now I wish to point out that in the case of both the oil and gas industry and the mining industry the rates or percentages of income, by which the depletion

allowances were measured, were arrived at by means of extensive studies conducted by the Bureau of Internal Revenue and the staff of the Joint Committee on Internal Revenue Taxation. Also, these rates were fully supported by studies made by the industries themselves. Furthermore, and in each instance, the rates finally fixed by Congress were considerably less than the percentage which the depletion allowance under the prior system bore to the taxpayers gross income.

S. Rep. No. 1631

(77th Cong., 2d Sess. (1942) (1942-2 Cum. Bull.) 504  
[to accompany H.R. 7378])

[65] DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL.

[115] SECTION 147. PERCENTAGE DEPLETION FOR COAL, FLUORSPAR, AND METAL MINES AND SULPHUR

This section is identical with section 131 of the House bill.

This amendment provides that fluorspar mines are to be allowed percentage depletion at a rate of 15 per cent, *subject to the same limitations as are applicable in the case of metal mines.* For taxable years beginning after December 31, 1941, the depletion deduction for coal, fluorspar, metal, and sulphur mines may be computed (without regard to any election) either on the percentage basis or on the cost basis, whichever gives the greater deduction. [Italics supplied.]



Senate debate, 1942

## (88 Cong. Record (Part 6))

[8033] Mr. THOMAS of Idaho. When the amendments providing for percentage depletion were under consideration in 1932, it was our understanding that *the ordinary treatment processes which a mine operator would normally apply in order to obtain a suitable product should be considered as a part of the mining operation.* Is any change in that law proposed at this time? [Italics supplied.]

Mr. JOHNSON of Colorado. Mr. President, I am glad the Senator brought up that subject, because it is one in which the Senator from Colorado has been very much interested, and it has been discussed in the Senate Finance Committee at considerable length. I am especially interested in the beneficiation of quicksilver, although no quicksilver is produced in the State of Colorado. But we have been met with this sort of situation with respect to quicksilver. If the producers of quicksilver will follow a certain process of beneficiation, they will receive the benefits of depletion fully, but if they adopt a more scientific method and a more modern method, then, of course, they run immediately into certain difficulties. That, to me, is something which is directly opposed to the public interest, and especially when we need quicksilver as badly as we do.

The question of what constitutes net income attributable to the mining of strategic metals and the companion questions regarding gross and net income from the property for percentage depletion have been considered with Mr. Randolph Paul, who has represented the Treasury before the Finance Committee on this subject. Mr. Paul urged that this was a subject which should be covered by Treasury regulations rather than

by detailed provisions of the law. *I agree that the statutes should not be burdened with regulatory details to fit every possible contingency.* I hope the Senator from Idaho will not offer an amendment on the subject at this time. [Italics supplied.]

*The Congress has not intended in the pending measure to make any change in its concept of mining income from that expressed in the 1932 and 1934 acts, nor to establish by implication or otherwise any approval of Treasury regulation or Revenue Bureau practice which departs from the original acts or the general Bureau practice prior to 1940.* [Italics supplied.]

I have conferred with Mr. Paul and he has stated to me the Treasury's intention to adhere to the original regulations and procedures under these acts, so that concentration by gravity or flotation and equivalent processes would be considered as part of the mining operation. Thus, for example, the furnacing of quicksilver ores would be considered as an equivalent of concentration by gravity or flotation.

Mr. Paul made only one *exception* to the *original regulations*; namely, that there would be excluded from gross income from the property *not only the cost of further processes such as smelting, but also the profits if any, attributable thereto*; intending thus to make the charges for a mining company's own smelter compare with those of an independent custom smelter. [Italics supplied.]

Mr. President, does that explain the situation to the Senator from Idaho, and is he satisfied with the explanation?

Mr. THOMAS of Idaho. Mr. President, I think with that explanation the situation is entirely satisfactory. What I was particularly anxious to know was whether the provision in question would make any changes in

the matter of depletion on the operations to which I referred. I was very active in 1932 in connection with the passage of the legislation on the subject. The same system is still being followed, I understand.

Mr. JOHNSON of Colorado. *Yes; the same system is being followed.* I know the Senator from Idaho took a very active part in having the legislation adopted in 1932. The Senator himself sponsored an amendment with respect to depletion in connection with the mining operations to which he referred. [Italics supplied.]

Revenue Act of 1942

(c. 619, 56 Stat. 798)

SEC. 145. PERCENTAGE DEPLETION FOR COAL, FLUORSPAR, BALL AND SAGGER CLAY, ROCK ASPHALT, AND METAL MINES AND SULPHUR.

(a) *Percentage Depletion.*—Section 114(b)(4) is amended to read as follows:

“(4) *Percentage Depletion for Coal, Fluorspar, Ball and Sagger Clay, Rock Asphalt, and Metal Mines and Sulphur.*—The allowance for depletion under section 23(m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, fluorspar, ball and sagger clay or rock asphalt mines, 15 per centum, and, in the case of sulphur mines or deposits, 23 per centum, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance under section 23(m) be less than it would be if computed without reference to this paragraph.”

(b) *Discovery Depletion Not Applicable to Fluorspar, Ball and Sagger Clay or Rock Asphalt Mines.*—Section 114(b)(2) is amended by striking out “metal, coal, or sulphur mines” and inserting in lieu thereof “metal, coal, fluorspar, ball and sagger clay, rock asphalt, or sulphur mines”.

1943

[Section 124 of the Revenue Act of 1943, c. 63, 58 Stat. 21, 44, added to the definition of “gross income from the property” to Code Section 114(b)(4) and in addition granted percentage depletion to certain critical minerals for the duration of the war. The definition of “gross income from the property” originated in the Senate and was revised in conference. The pertinent legislative reports, hearings, congressional debate, as well as the amending statute and the amended Treasury Regulations promulgated thereunder, are set forth below in chronological order.]

H. Rep. No. 871

(78th Cong., 1st Sess. (1944 Cum. Bull. 901))

[48] SEC. 114. Percentage Depletion for Flake Graphite, Vermiculite, Potash, Beryl, Feldspar, Mica, Lepidolite, and Spodumene.

Subsection (a) of this section amends the heading and the first sentence of section 114(b)(4), relating to percentage depletion for coal, fluorspar, ball and sagger clay, rock asphalt, and metal mines, and sulphur, so as to include among the mines or deposits entitled to percentage depletion flake graphite, vermiculite, beryl, feldspar, mica, lepidolite, spodumene, and potash. In the case of flake graphite, vermiculite, beryl, feldspar, mica, lepidolite, and spodumene mines, the

allowance for depletion shall be 15 percent, and in the case of potash mines or deposits, the allowance for depletion shall be 23 percent, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. This allowance is subject to the further limitations contained in the existing provisions of section 114(b)(4).

Subsection (b) amends section 114(b)(2) relating to discovery value of certain mines, so as to debar the use of the discovery value as the basis for depletion in the case of flake graphite, vermiculite, beryl, feldspar, mica, lepidolite, spodumene, and potash mines.

Subsection (c) provides that the amendments made by subsections (a) and (b), insofar as they apply to flake graphite mines, shall be applicable to taxable years beginning after December 31, 1942.

Subsection (d) provides that the amendments made by subsections (a) and (b) and the amendments made to section 114 of the code by section 145 of the Revenue Act of 1942, providing percentage depletion for fluorspar, ball and sagger clay, and rock asphalt, shall not be applicable to any taxable year beginning on or after the date of the termination of hostilities.

**Senate Hearings, 1943**

(Revenue Act of 1943, Hearings before the Committee on Finance, United States Senate, 78th Cong., 1st Sess., on H.R. 3687)

[25] Statement of RANDOLPH PAUL, General Counsel of the Treasury:

[66]



The Treasury's position with respect to the extension of percentage depletion to strategic minerals as a wartime measure is the same as that with respect to the exemption of these minerals from excess-profits taxes. If, but only if, the allowance of percentage depletion for the duration of hostilities will contribute to the war effort, the Treasury recognizes the advantages of such allowances despite our firm conviction that the percentage depletion provisions in the present law have, in general, enabled many individual and [68] corporate taxpayers to avoid their fair share of the Nation's tax burden. Generally, our position with respect to percentage depletion is the same as was expressed in hearings on the 1942 revenue bill.<sup>1</sup>

However, on the basis of the representations of the War Production Board that percentage depletion for these metals for the duration of the war will contribute to the war effort, we concur in the action taken in the House bill in granting percentage depletion to fluor spar, flake graphite, sheet mica, and beryl.

On the other hand, the Treasury does not believe that the extension of percentage depletion to vermiculite, feldspar, lepidolite, spodumene, and potash can be justified even as a war measure. \* \* \*

\* \* \* \* \*

[527] Statement of DONALD H. McLAUGHLIN, representing the Tax Committee of the American Mining Congress:

Mr. McLAUGHLIN. Mr. Chairman, on behalf of the tax committee of the American Mining Congress, of which I am a member, I am speaking in support of the amendment introduced by Senator Johnson to the section of the revenue bill that pertains to gross in-

<sup>1</sup> See Secretary Morgenthau's statement, p. 8, and testimony of Randolph Paul, pp. 84, 2988, 3438, hearings before Ways and Means Committee, 77th Cong., 2d sess.

come from the property for purposes of percentage depletion.

When percentage depletion was introduced in the Revenue Act of 1932, the Treasury Regulations under which it was to be administered were the subject of conferences between Assistant Secretary Douglas and others of the Treasury Department, and representatives of the mining industry among whom I was included. The regulations then adopted have been preserved essentially in their present form as far as definition of "gross income" is concerned except for a single amendment in 1940 with regard to allocation of a portion of the profits of a mining enterprise to certain processes or operations to which reference will be made later.

*When the 1932 regulations were adopted, it was understood by the representatives of the mining industry that the omission of a complete recital of the many processes by which ores are beneficiated was simply to avoid burdening the regulations with a lengthy and possibly incomplete statement, and that the meaning of the act was met by the inclusion of phrases such as "other processes" which were deemed adequate to cover other common methods of treatment similar in their function to those specified. With the regulations in this form, it was believed that the administration of the law would not depart from what we had been informed was the intent of the Members of Congress who had sponsored the legislation. [Italics supplied.]*

This was clearly expressed later upon the floor of the Senate by Senator Thomas when in a discussion with Senator Johnson (p. 8291, vol. 88, Congressional Record, 77th Cong., 2d sess.), he said:

When the amendments providing for percentage depletion were under consideration in

1932, it was our understanding that the ordinary treatment processes, which a mine operator would normally apply in order to obtain a suitable product, should be considered as a part of the mining operation.

*That this understanding was well founded and expressed the agreement reached at this conference with Assistant Secretary Douglas is clearly borne out by the action of the Bureau of Internal Revenue for the next 8 years in accepting and settling tax returns based upon it. During this period, the law with regard to percentage depletion was repeatedly reenacted and the regulations remained essentially unchanged. For example, in the case of gold mines, common processes such as amalgamation and cyanidation were regarded as the equivalent of concentration by gravity or flotation, and no distinction was made between the tax return of a company employing the former as its major method of beneficiation and one that happened to find the latter better suited to its ores. [Italics supplied.]*

*In 1941, however, the Bureau unexpectedly took a position that implied it had been in error in the preceding years and claimed deficiencies in the returns of a number of companies for the years 1938, 1939, and 1940, which were the only ones still open for adjustment, by requiring that the cost of processes such as cyanidation in the case of gold ores and furnacing in the case of quicksilver ores [528] must be deducted in calculating gross income, upon which percentage depletion was based, on the grounds that these processes were not specifically mentioned in the regulations. This current stand of the Bureau is not based on any public statements, so it is difficult to know just how far it is intended to go in excluding one after another of the well recognized processes of beneficiation from the group that was formerly accepted as the*

equivalent of concentration by gravity or flotation, but from the various cases that have now arisen, the taxpayer cannot avoid feeling apprehensive that the term "other processes" in the regulations is no longer of any significance in the eyes of the Treasury. [Italics supplied.]

*The question of allotment of profits to specific processes of beneficiation was discussed at the conferences in 1932, but it was ruled out on account of the difficulties of administering it in a simple and equitable way not subject to controversy. In spite of these considerations that were regarded as compelling in 1932, provision for allotment of a portion of the profits to processes subsequent to those mentioned was made in the regulations issued in 1940 and applied in the claims for deficiencies to which reference is made above. [Italics supplied.]*

As a result, the differences in treatment of taxpayers, even in the same type of mining operations, have been so great and inequitable that the wisdom of the early decision to keep the administration of the law on as simple a basis as possible has been confirmed in a most positive way.

*The proposed amendment simply incorporates in the law the practices established by the Bureau under the 1932 regulations, and does not modify the existing regulations in any essential way except to limit the deductions in calculating gross income to the costs of the processes or services subsequent to those which are regarded as ordinary treatment processes and specifically stated as such. [Italics supplied.]*

*The clarification of the law that would be accomplished by this amendment would relieve many taxpayers not only of uncertainties with regard to their tax liabilities but also with regard to choice of technical practices, for the present policies of the Bureau*

create such discriminations between processes designed to accomplish identical ends that a taxpayer might feel compelled to replace an entirely satisfactory plant with one of a type that now happens to be specifically mentioned in the regulations. [Italics supplied.]

Consequently, I feel strongly that *in the interest of fair treatment as between taxpayers in the mining industry and simplicity in the administration of the revenue act* it is imperative to remove these sources of uncertainty and conflict by adopting the proposed amendment that *restores Treasury procedure to that which was originally intended by Congress and that makes unmistakably clear just what can and what cannot be deducted from the value of the output of mines in calculating their depletion base.* [Italics supplied.]

(The amendment by SENATOR JOHNSON, referred to above, is as follows:)

[529] Amendment intended to be proposed by Mr. JOHNSON of Colorado to the bill (H.R. 3687) to provide revenue, and for other purposes, viz: at the proper place, insert the following:

**SEC.—Gross Income From Property for Purposes of Percentage Depletion.**

(a) Section 114(b)(4) is amended by adding at the end thereof a new subparagraph, (B), to read as follows:

“(B) Definition of Gross Income From Property.—As used in this paragraph the term ‘gross income from the property’ means the gross income from mining. The term ‘mining’, as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine



owners or operators in order to obtain the commercially marketable mineral product or products. The term 'ordinary treatment processes' as used herein, shall include the following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulfur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, precipitation (but not including electrolytic deposition), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores. In the determination of such gross income from mining, there shall be excluded the costs of any process or service which does not constitute an ordinary treatment process. The principles of this subparagraph shall also be applicable in determining gross income attributable to mining for the purposes of sections 731 and 735."

(b) the amendment made by subsection (a) hereof shall be effective as of the date of enactment of the Internal Revenue Code.

(c) Section 114(b)(4) of the Revenue Act of 1938 and the corresponding provisions of the Revenue Acts of 1936, 1934, and 1932, as amended, are hereby amended by inserting therein the amendment con-

tained in subsection (a), other than the last sentence thereof, such amendment to be effective as of the date of enactment of each of the respective Acts.

[785] Statement of GORDON G. CROWDER, Chairman, Special Tax Committee, National Coal Association:

[786]

Seventh, Senator Johnson of Colorado has proposed an amendment to the pending bill to provide a proper definition of gross income from property for purposes of percentage depletion. Senator Thomas of Oklahoma has proposed an amendment to the pending bill dealing with termination of percentage depletion for certain minerals. The National Coal Association supports these amendments and urges that the committee adopt them.

[839]

SENATOR WALSH. A memorandum for inclusion in the record has been submitted by Mr. A. T. Kearney of the committee of vermiculite miners which will be inserted in the record at this point.

(The memorandum referred to is as follows:)

[842] Summary of Memorandum Regarding Percentage Depletion for Vermiculite:

1. Vermiculite is a nonmetallic mineral found in North and South Carolina, Colorado, Texas, Montana, and Wyoming.

2. The War Production Board has reported to the Ways and Means Committee that its continued production is essential to the war effort.

3. Vermiculite, a fireproof insulating material, is used principally in the war effort for combat war planes, airplane engine test sheds, oilless bearings for tanks, ship decking, fireproof bulkheads for ships, sound-deadening and insulating materials for walls, floors, and roof decks for hospitals, Army and Navy camps, and other types of war buildings.

4. Estimated 1943 production will be about 46,000 tons. Estimated demand for 1943 will be in excess of 65,000 tons.

[842] 9. Processors and fabricators who purchase ore from vermiculite miners have invested more than \$2,000,000 in their businesses. Estimated sales in 1942 by processors, fabricators, and dealers exceeded \$6,000,000, on which total estimated income taxes in excess of \$200,000 were paid.

10. If percentage depletion were permitted *miners*, a steady flow of a *basic material* to *fabricators* and *processors* would be assured. This would serve the war effort, continue tax revenue presently being collected from that source, and, in addition, would provide increase in tax revenue from processors, fabricators, and dealers which would more than offset any loss of revenue from vermiculite miners. [Italics supplied.]

11. The Ways and Means Committee have voted to include vermiculite in the new revenue act with those minerals on which 15 percent depletion is allowed.

[926]. Statement of HENRY B. FERNALD, Chairman, Tax Committee, American Mining Congress:

Mr. FERNALD. Mr. Chairman, on behalf of the mining industry we submit the following statement re-

garding certain features to which we urge your attention in connection with the pending tax bill.

[927]

\* \* \* \* \*

We believe Congress has intended to recognize fully the need for capital allowances for mines so that there should be taxed as income or as excess profits only that which remains after full capital allowances. In the framing of our laws and their application by the Treasury that intent is not being fully observed. This is not a quibble over particular words or phrases and their interpretation, but it is a matter of substance and practical application. So we call to your attention certain points where amendment of the law seems necessary to express what we believe was the congressional intent that the exceedingly [928] high rates imposed on taxable income should not be applied to capital realization:

1. Gross income from the property: The allowances for percentage depletion and the excess-profits tax exemptions of strategic minerals, of above-quota bonus and of excess output, all depend to a considerable extent on the definition of "gross income from the property." *There is immediate need for writing into the law a definition which will express the congressional intent. This has been the subject of special presentation to you by Dr. Donald H. McLaughlin in which he has explained to you why we so strongly urge the adoption of the amendment which Senator Johnson has proposed.* [Italics supplied.]

\* \* \* \* \*

(78th Cong., 1st Sess. (1944 Cum. Bull. 973))

[23]

### PERCENTAGE DEPLETION

Under the House bill, percentage depletion is extended to flake graphite, vermiculite, potash, beryl, feldspar, mica, lepidolite, and spodumene, in addition to those minerals presently receiving it, and discovery depletion is consequently terminated with respect to these minerals. The extension to flake graphite applies to years beginning after December 31, 1942, but the extensions made by this bill and the Revenue Act of 1942 are limited to the duration of the war.

Your committee makes three changes in this provision. It includes a mineral by the name of talc, and in the case of potash, it reduces the rate from 23 percent to 15 percent and makes the allowance permanent and not limited to the duration of the war.

### DECLARATION OF GROSS INCOME FROM THE PROPERTY IN THE CASE OF PERCENTAGE DEPLETION

Section 114(b)(4) of the code is amended to include a definition of "gross income from the property" for purposes of percentage depletion of mines. It also defines the scope of income from mining for the purposes of section 731 and section 735. *The purpose of the provision is to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation, and to give reasonable specification of what are to be considered such processes for various kinds or classes of mines. [Italics supplied.]*



The law has never contained such a definition, and its absence has given rise to numerous disputes. *The definition here prescribed expresses the congressional intent of these provisions as first included in the law, and is in accord with the original regulations and the [24] Bureau practices and procedures thereunder. It is therefore made retroactive to the date of such original provisions. [Italics supplied.]*

[39] DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL

TITLE 1.—INDIVIDUAL AND CORPORATION INCOME TAXES

[54]

Sec. 117. Percentage Depletion for Flake Graphite, Vermiculite, Potash, Beryl, Feldspar, Mica, Tale, Lepidolite, and Spodumene.

This section is substantially similar to Section 114 of the House bill but differs in some respects as hereinafter discussed.

Subsection (a) of this section amends the heading and the first sentence of section 114(b)(4), relating to percentage depletion for coal, fluorspar, ball and sagger clay, rock asphalt, and metal mines, and sulphur, so as to include among the mines or deposits entitled to percentage depletion flake graphite, vermiculite, beryl, feldspar, mica, tale, lepidolite, spodumene, and potash. The provision relating to tale was not in the House bill. In the case of flake graphite, vermiculite, potash, beryl, feldspar, mica, tale, lepidolite, and spodumene mines, the allowance for depletion shall be 15 percent of the gross income from the property during the taxable year, excluding from such gross

income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property. This allowance is subject to the further limitations contained in the existing provisions of section 114(b)(4). The provision in the House bill fixing the allowance in the case of potash at 23 percent has been eliminated.

Subsection (b) amends section 114(b)(2) relating to discovery value of certain mines, so as to debar the use of the discovery value as the basis for depletion in the case of flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, and potash mines. As noted above, talc was not included in the House bill provision.

[55] Subsection (c), which was not in the House bill, adds a new subparagraph (B) to section 114(b)(4) of the code to define for the purposes of section 114(b)(4) the term "gross income from the property." For such purposes the term "gross income from the property" means the gross income from mining. The term "mining" shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products. It is further provided that the term "ordinary treatment processes," as so used, shall include the following:

(1) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (2) in the case of sulfur—pumping to vats, cooling, breaking, and loading for shipment; (3) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for ship-

ment; and (4) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, precipitation (but not including electrolytic deposition), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quick-silver ores. The costs of any process or service which does not constitute an “ordinary treatment process” shall be excluded in the determination of such gross income from mining. Provision is also made that the principles of this subparagraph shall be applicable in determining gross income attributable to mining for the purposes of section 731 of the code (relating to corporations engaged in mining of strategic minerals) and section 735 of the code (relating to nontaxable income from certain mining and timber operations).

Subsection (d) provides that the amendments made by subsections (a) and (b), insofar as they apply to flake graphite mines, shall be applicable to taxable years beginning after December 31, 1942.

Subsection (e) of the House bill provides that the amendments made by subsections (a) and (b) and the amendments made to section 114 of the code by section 145 of the Revenue Act of 1942, providing percentage depletion for fluorspar, ball and sagger clay, and rock asphalt, shall not be applicable to any taxable year beginning on or after the date of the termination of hostilities. Your committee has amended this subsection to provide that the termination date applicable to the minerals specified in subsections (a) and (b) shall not be applicable in the

case of potash. Your committee has also provided that the amendment made by subsection (c) of this section shall be effective as if it were a part of the Internal Revenue Code and the Revenue Acts of 1938, 1936, 1934, and 1932, as of the effective date of the code and as of the date of enactment of each of the respective acts.

Senate Debates, 1944

(90 Cong. Record (Part 1), 78th Cong., 2d Sess.)

[85]

### THE REVENUE ACT

The Senate resumed the consideration of the bill (H.R. 3687) to provide revenue, and for other purposes.

[99]

The next amendment was, on page 59, in line 12, after the word "sulphur", to strike out "or potash", and in line 21, after the word "mica", to insert "talc."

The amendment was agreed to.

The next amendment was, on page 59, after line 21, to insert:

(c) **Definition of gross income from the property:** Section 114(b)(4) is amended by adding at the end thereof the following:

(B) **Definition of gross income from property:** As used in this paragraph the term "gross income from the property" means the gross income from mining. The term "mining," as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products. The term "ordinary treatment processes," as used

herein, shall include the following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulfur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the case of lead, zinc, copper, gold, silver, or fluorspar [100] ores, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, precipitation (but not including electrolytic deposition), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores. In the determination of such gross income from mining, there shall be excluded the costs of any process or service which does not constitute an ordinary treatment process. The principles of this subparagraph shall also be applicable in determining gross income attributable to mining for the purposes of sections 731 and 735.

Mr. HATCH. Mr. President, I send to the desk an amendment to the committee amendment, which I offer and ask to have stated. It has the same purpose, that of merely clarifying and correcting what appear to be technical errors.

The PRESIDING OFFICER. The amendment to the amendment will be stated.

The CHIEF CLERK. To the committee amendment, on page 60, in line 21, before the word "and", it is proposed to insert the word "potash."

The PRESIDING OFFICER. The question is on agree-



ing to the amendment offered by the Senator from New Mexico to the committee amendment.

The amendment to the amendment was agreed to.

Mr. HATCH. Mr. President, I offer and send to the desk another amendment to the committee amendment on page 60. The amendment is of the same nature as the former one. *It would merely add the word "crystallization," a change which is a matter of technical wording.* [Italics supplied.]

The PRESIDING OFFICER. The amendment offered by the Senator from New Mexico to the committee amendment will be stated.

The CHIEF CLERK. At the end of the committee amendment on page 60, in line 25, it is proposed to insert the word "crystallization" and a comma.

The PRESIDING OFFICER. The question is on agreeing to the amendment of the Senator from New Mexico to the committee amendment.

The amendment to the amendment was agreed to.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment as amended.

The amendment as amended was agreed to.

Mr. HATCH. Mr. President, some time ago I submitted an amendment and asked that it be referred to the Committee on Finance. It related primarily to potash. The committee adopted a part of the amendment which I submitted. However, the amendment which I submitted included two sections. I did not argue before the committee the second section, which reads as follows:

(c) Income from potash mines or deposits: Section 114(b)(4) is amended by adding at the end thereof the following sentence: "In the case of potash, whether extracted from a mine or from a brine or other deposit, there shall be

included in gross and net income from the property the income from other minerals or mineral salts extracted therefrom."

\* \* \* \* \*

Mr. GEORGE. I am not familiar with it. I am willing to take it to conference, with the understanding that we shall there have the right fully to examine it.

Mr. HATCH. That is satisfactory.

The PRESIDING OFFICER. The amendment offered by the Senator from New Mexico will be stated.

\* \* \* \* \*

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from New Mexico [Mr. HATCH].

The amendment was agreed to.

The PRESIDING OFFICER. The question is on agreeing to the committee amendment on page 61, line 25.

The amendment was agreed to.

\* \* \* \* \*

[194] Mr. McCLELLAN. Mr. President, I ask unanimous consent to return to pages 58 and 59 of the bill, section 117, I offer the amendments which I send to the desk and ask to have read.

The PRESIDING OFFICER. Without objection, the amendments will be stated.

The CHIEF CLERK. The following amendments are proposed:

On page 58, lines 20 and 21, strike out "and spodumene" and insert "spodumene, and barite."

On page 59, line 5, after "spodumene", insert "barite."

On page 59, line 11, after "spodumene", insert "barite."

On page 59, line 21, after "spodumene", insert "barite."

Mr. McCLELLAN. Mr. President, the amendments, or substantially these, were presented by me to the Finance Committee. That was in the closing days of the committee's consideration of the bill, and the matter had come to my attention only at that time. The committee suggested that I secure from the War Production Board a statement or certificate with respect to this mineral and its importance—in other words, the War Production Board's recommendation regarding whether it should be included along with other minerals and metals which now are included in subsection 4 of section 117 of the pending bill, to receive the benefit of percentage depletion.

I immediately took up the matter with the War Production Board, and was advised by letter of December 21, the letter being written by Mr. Harry J. Wolf, chief of the Cadmium-Indium Section, Zinc Division, of the War Production Board. \* \* \*

\* \* \* \* \*

[195] Mr. GEORGE. Mr. President, I will not object to the amendment, because the letter submitted by the distinguished junior Senator from Arkansas, which he received from the War Production Board, is unusually strong.

There has been opposition by many members of the committee to the inclusion of certain minerals in the provision with respect to the depletion allowance. It is questionable whether the policy on which we have embarked is sound, but the House has included several new metals and minerals and given them a depletion allowance. The Senator from Arkansas has certainly made a meritorious case in this particular instance. I will not offer any objection to the amendment.

The PRESIDING OFFICER. The question is on agreeing to the amendment offered by the Senator from Arkansas [Mr. McCLELLAN].

The amendment was agreed to.

H. Conference Rep. No. 1079

(78th Cong., 2d Sess. (1944 Cum. Bull. 1059))

[20] \* \* \* \* \*

Amendment numbered 47: That the House recede from its disagreement to the amendment of the Senate numbered 47, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

[21] (c) DEFINITION OF GROSS INCOME FROM THE PROPERTY.—Section 114(b)(4) is amended by adding at the end thereof the following:

“(B) Definition of Gross Income From Property.—As used in this paragraph the term ‘gross income from the property’ means the gross income from mining. The term ‘mining’, as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products. The term ‘ordinary treatment processes’, as used herein, shall include the following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulfur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing,

grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores. The principles of this subparagraph shall also be applicable in determining gross income attributable to mining for the purposes of sections 731 and 735."

And the Senate agree to the same.

Amendment numbered 49: That the House recede from its disagreement to the amendment of the Senate numbered 49, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert A provision having the effect of the amendment made by subsection (c) shall be deemed to be included in the revenue laws respectively applicable to taxable years beginning after December 31, 1931.; and the Senate agree to the same.

[40] STATEMENT OF THE MANAGERS ON THE PART  
OF THE HOUSE:

The managers on the part of the House at the conference on the disagreeing votes of the two Houses on the amendments of the Senate to the bill (H.R. 3687) to provide revenue, and for other purposes, submit the following statement in explanation of the effect of the action agreed upon by the conferees and recommended in the accompanying conference report:



[50]

Amendments Nos. 37, 38, 39, 41, 42, 45, and 46. These amendments made to section 114 of the House bill include talc and barite in the list of mines which are entitled to depletion at the rate of 15 percent of the gross income from the property (subject to other limitations in the code), and exclude talc and barite from the list of mines entitled to depletion based on discovery value. These amendments do not apply with respect to any taxable year beginning on or after the date of the termination of hostilities in the present war, as defined in subsection (e) of this section. The House recedes as to these amendments with a clerical amendment to amendment No. 37 changing the section heading.

Amendments Nos. 40, 48, and 50: These are clerical amendments. The House recedes as to these amendments with a clerical change in amendment No. 40.

Amendments Nos. 43, 44, and 51: Under section 114 of the House bill, potash mines and deposits were allowed percentage depletion in an amount equal to 23 percent of the gross income from the property (subject to other limitations in the code), and were excluded from the list of mines entitled to discovery value depletion; these provisions were not to be applicable to any taxable year beginning on or after the date of the termination of hostilities in the present war. These amendments provide that potash mines or deposits shall be allowed [51] depletion based upon 15 percent of the gross income from the property, instead of 23 percent, and remove the restriction contained in the House bill which would make inapplicable such allowance for taxable years beginning on or after the date of the termination of hostilities in the present war. It is contemplated that the regulations to be issued by the Commissioner will

provide that potash salts in solution are deemed to be a natural deposit. The House recedes.

Amendments Nos. 47 and 49: For the purposes of section 114(b)(4) of the code amendment No. 47 defines the term "gross income from the property" upon which is based the allowance for percentage depletion. Thus "gross income from the property" means gross income from "mining," and "mining" is considered to include the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products as well as the extraction of the ores or minerals from the ground. *The costs of any process or service which does not constitute an ordinary treatment process is to be excluded in determining gross income from mining.* Several specified processes have been listed as being included in the term "ordinary treatment processes." The principles set forth in this amendment are made expressly applicable to mining for the purposes of sections 731 and 735 of the code. Amendment No. 49 makes amendment No. 47 effective as if it were a part of the Internal Revenue Code and the Revenue Acts of 1938, 1936, 1934, and 1932 on the date of their respective enactments. *The House recedes with amendments which strike out the next to the last sentence of the subparagraph added by amendment No. 47, which provided that the costs of any process or service which does not constitute an ordinary treatment process is to be excluded in determining gross income from mining, and with an amendment excluding electrolytic deposition, roasting, thermal or electric smelting and refining from the definition of "ordinary treatment processes" and which rephrase the retroactivity provisions in amendment No. 49. [Italics supplied.]*

Amendment No. 52: This amendment, for which there is no corresponding provision in the House bill,

provides that, in computing percentage depletion under section 114(b)(4) of the code in the case of potash (whether extracted from a mine or from a brine or other deposit), there shall be included in gross and net income from the property the income from other minerals or mineral salts extracted from such property. The Senate recedes.

Revenue Act of 1943

(c. 63, 58 Stat. 21, 44)

**SEC. 124. PERCENTAGE DEPLETION FOR FLAKE GRAPHITE, VERMICULITE, POTASH, BERYL, FELDSPAR, MICA, TALC, BARITE, LEPIDOLITE, AND SPODUMENE.**

(a) *In General.*—So much of section 114(b)(4) (relating to percentage depletion for certain minerals) as precedes the second sentence thereof is amended to read as follows:

*(4) Percentage Depletion for Coal, Fluorspar, Flake Graphite, Vermiculite, Beryl, Feldspar, Mica, Talc, Lepidolite, Spodumene, Barite, Ball and Sagger Clay, Rock Asphalt, and Metal Mines, Potash, and Sulphur.*—

(A) *In General.*—The allowance for depletion under section 23(m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, fluorspar, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, ball and sagger clay, or rock asphalt mines, and potash mines or deposits, 15 per centum, and in the case of sulphur mines or deposits, 23 per centum, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property.

(b) *Discovery Value.*—Section 114(b)(2) (relating to discovery value) is amended by inserting after

"fluorspar" the following: "flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, potash,".

(c) *Definition of Gross Income From the Property*.—Section 114(b)(4) is amended by adding at the end thereof the following:

(B) *Definition of Gross Income From Property*.—As used in this paragraph the term "gross income from the property" means the gross income from mining. The term "mining", as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products. The term "ordinary treatment processes", as used herein, shall include the following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product

or products from the ore, including the furnacing of quicksilver ores. The principles of this subparagraph shall also be applicable in determining gross income attributable to mining for the purposes of sections 731 and 735.

(d) *Percentage Depletion for Flake Graphite Retroactive to 1943.*—The amendments made by subsections (a) and (b) inserting flake graphite in section 114(b) (2) and (4) of the Internal Revenue Code shall be applicable with respect to taxable years beginning after December 31, 1942. A provision having the effect of the amendment made by subsection (c) shall be deemed to be included in the revenue laws respectively applicable to taxable years beginning after December 31, 1931.

(e) *Termination of Percentage Depletion for Certain Minerals.*—The amendments made by subsections (a) and (b) (except as they relate to potash) and the amendments made to section 114 of the Internal Revenue Code by section 145 of the Revenue Act of 1942 (providing percentage depletion for fluorspar, ball and sagger clay, and rock asphalt), shall not apply with respect to any taxable year beginning on or after the date of the termination of hostilities in the present war. For the purposes of this subsection the term "date of the termination of hostilities in the present war" means the date proclaimed by the President as the date of such termination, or the date specified in a concurrent resolution of the two Houses of Congress as the date of such termination, whichever is the earlier.



## Treasury Regulations 111

(Effective for years beginning after December 31, 1941, as first amended after passage of 1943 Act)

SEC. 29.23(m)-1 [as amended by T.D. 5413, approved October 31, 1944 (1944 Cum. Bull. 124)].  
*Depletion of mines, oil and gas wells, other natural deposits, and timber; depreciation of improvements.—*

Section 23(m) provides that there shall be allowed as a deduction in computing net income in the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements. Section 114 prescribes the bases upon which depreciation and depletion are to be allowed.

When used in these sections (29.23(m)-1 to 29.23(m)-28, inclusive) covering depletion and depreciation—

(d) "Minerals" include ores of the metals, coal, oil, gas, and such nonmetallic substances as abrasives, asbestos, asphaltum, *barite*, *beryl*, borax, building stone, cement rock, clay, crushed stone, feldspar, fluorspar, fuller's earth, graphite, gravel, gypsum, *lepidolite*, limestone, magnesite, marl, mica, mineral, pigments, peat, potash, precious stones, refractories, rock phosphate, salt, sand, silica, slate, soapstone, soda, *spodumene*, sulphur, talc, and *vermiculite*. [Italics supplied.]

(f) The term "gross income from the property," as used in sections 114(b)(3) and 114(b)(4)(A) and sections 29.23(m)-1 to 29.23(m)-28, inclusive, means the following:

*In the case of oil and gas wells, "gross income from*

*the property*" as used in section 114(b)(3) means the amount for which the taxpayer sells the oil and gas in the immediate vicinity of the well. If the oil and gas are not sold on the property but are manufactured or converted into a refined product prior to sale, or are transported from the property prior to sale, the gross income from the property shall be assumed to be equivalent to the representative market or field price (as of the date of sale) of the oil and gas before conversion or transportation.

In the case of a crude mineral product other than oil and gas, "*gross income from the property*", as used in section 114(b)(4)(A) means the gross income from mining. The term "*mining*" as used herein includes not only the extraction of ores or minerals from the ground but also the ordinary treatment processes which are normally applied by the mine owners or operators to the crude mineral product after extraction in order to obtain the commercially marketable mineral product or products. [Italics supplied.]

If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "*gross income from the property*" means the amount for which such product was sold, but, if the product is transported or processed (other than by the ordinary treatment processes described below) before sale, "*gross income from the property*" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as *beneficiated by the ordinary treatment processes actually applied*, before transportation of such product. If there is no such representative market or field price (as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in

its crude mineral state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation and the processes *beyond the ordinary treatment processes.* [Italics supplied.]

The term "ordinary treatment processes," as used herein, shall include the following:

- (1) In the case of coal—cleaning, breaking, sizing, and loading for shipment;
- (2) In the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment;
- (3) In the case of iron ore, *bauxite*, ball and sagger clay, rock asphalt, and *minerals* which are customarily sold in the form of a crude mineral product—sorting, concentrating, and *sintering* to bring to shipping grade and form, and loading for shipment;
- (4) In the case of lead, zinc, copper, gold, silver, or fluorspar ores, *potash*, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding and *beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore.* The furnacing of quicksilver ores is included in the term "ordinary treatment processes." The following processes are not included in the term "ordinary treatment processes"; electrolytic deposition, roasting, thermal or electric smelting, refining, or *substantially equivalent processes.* [Italics supplied.]

In case any of the ordinary treatment processes are not applied in the immediate vicinity of the mining district in which the mine is located, costs incurred for transportation to the processing location and, if transported by the taxpayer, the proportionate profits

attributable to transportation, should be subtracted from the sale price of the product to determine "gross income from the property."

(g) "Net income of the taxpayer (computed without allowance for depletion) from the property," as used in section 114(b)(2), (3), and (4) and sections 29.23(m)-1 to 29.23(m)-28, inclusive, means the "gross income from the property" as defined in paragraph (f) of this section less the allowable deductions attributable to the mineral property upon which the depletion is claimed and the allowable deductions attributable to the processes listed in paragraph (f) in so far as they relate to the product of such property, including overhead and operating expenses, development costs properly charged to expense, depreciation, taxes, losses sustained, etc., but excluding any allowance for depletion. Deductions not directly attributable to particular properties or processes shall be fairly allocated. To illustrate: In cases where the taxpayer engages in activities in addition to mineral extraction and to the processes listed in paragraph (f), deductions for depreciation, taxes, general expenses, and overhead, which cannot be directly attributed to any specific activity, shall be fairly apportioned between (1) the mineral extraction and the processes listed in paragraph (f) and (2) the additional activities, taking into account the ratio which the operating expenses directly attributable to the mineral extraction and the processes listed in paragraph (f) bear to the operating expenses directly attributable to the additional activities. If more than one mineral property is involved, the deductions apportioned to the mineral extraction and the processes listed in paragraph (f) shall, in turn, be fairly apportioned to the several

properties, taking into account their relative production.

(h) "Crude mineral product," as used in paragraph (f) of this section, means the product in the form in which it emerges from the mine or well.

1945

T.D. 5461

(Approved July 9, 1945 (1945 Cum. Bull. 284))

[This added the following sentence to Treasury Regulations 111, Section 29.23(m)-1(f)]

If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method.

1947

[The Act of August 8, 1947, c. 515, 61 Stat. 917, Section 15, repealed the provision limiting percentage depletion for certain non-metallies to the war-time period, and added certain other non-metallies to the list for which percentage depletion was allowed. Passage of the Act was preceded by a House hearing in which several mining industries were represented. The portions of their statements relating to the processes applied by the industry to the particular mineral are included in Part B of this appendix, but the proceedings leading up to the passage of the Act are otherwise given below in chronological order.]



(Percentage Depletion, Hearing before the Committee on Ways and Means, House of Representatives, 80th Cong., 1st Sess., on H.R. 1993 (1947))

[1] Statement of MALCOLM TARVER, representing the Committee on Taxation, Barite Industry of the United States:

[2] The bills seek to renew the provisions of section 124 of the Revenue Act of 1943, relating to the depletion tax credit for nonmetallic ores.

It is, of course, unnecessary that I should undertake to discuss before members of this committee, which has studied this question and accorded it consideration throughout the years, the technical features which are involved in this proposition.

I do wish, however, to point out to you certain salient facts which to my mind constitute incontrovertible arguments in favor of the enactment of this legislation.

[11] Mr. SIMPSON. Judge Tarver, have you any figures to indicate approximately how much per ton this depletion allowance may amount to, allowed by the tax laws at the present time?

Mr. TARVER. The cost of production, f.o.b. the mines, is approximately \$8 per ton, and the 15 percent depletion allowance is *upon the gross value of production, as I understand it.* (Italics supplied.)

[14] Statement of WESLEY E. DISNEY, Tulsa, Okla., representing the talc, fluorspar, and thenardite interests:

I would like to stress one thing that Judge Tarver referred to, and that is the question of discrimination.

[15] Every one of these items, except thenardite, which is mined in a manner similar to sulfur—every one of these nonmetallics is a mining operation.

All of the mineral ores have percentage depletion of 15 percent. Very little dissimilarity in the operation of producing and processing these ores to the mining and processing of the minerals that all enjoy a 15-percent depletion under long-existing statutes exists.

\* \* \*  
[18] Mr. DISNEY. As I said, I do not want to take the committee's time. Let me make quick reference to fluorspar for a moment.

It was given permanent depletion through the 1942 act, and through some error it got into the termination clause.

\* \* \*  
Mr. LYNCH. This talc and the other mineral interests that you represent here—as I understand it, they are all mined, are they not?

Mr. DISNEY. Talc and fluorspar, yes; they are mined.

Mr. LYNCH. It is a mining operation?

Mr. DISNEY. Yes. The operation for that thenardite is similar to the sulfur operation.

Mr. LYNCH. What you are asking for here in reality is to have the same treatment afforded to these particular interests as has been accorded to other metals or other ores?

Mr. DISNEY. Yes, sir, as they were up to the 1st of last January, and mineral ores have been accorded that type of treatment for many years, including coal.

Mr. LYNCH. *So there is no change in principle here?* [Italics supplied.]

Mr. DISNEY. *None whatever.* [Italics supplied.]

Mr. LYNCH. *It is just applying the old principle to these minerals which previously had this depletion percentage?* [Italics supplied.]

Mr. DISNEY. *Yes; they had it.* Fluorspar had it from 1942 up until the 1st of last January, and the others from 1943 to 1946, inclusive. [Italics supplied.]

Mr. LYNCH. *'Aside from the time period, the principle is just the same?* [Italics supplied.]

Mr. DISNEY. *It is exactly the same.* [Italics supplied.]

Mr. LYNCH. *It is the same with respect to these minerals as with respect to oil and other minerals which have percentage depletion?* [Italics supplied.]

Mr. DISNEY. *That is true sir.* [Italics supplied.]

\* \* \* \* \*

[25] Statement in support of percentage depletion for talc producers before the Ways and Means Committee of the House of Representatives, June 4, 1947:

My name is HENRY MULRYAN of Glendale, Calif. \* \* \*

\* \* \* \* \*

I wish to present a brief description of talc, how and where it is mined, its characteristics and uses, and why its producers should have the benefit of percentage depletion made a permanent part of the income tax law.

\* \* \* \* \*

[27] There are numerous reasons why percentage depletion should be permanent for talc. The industry fails to see any essential difference between the mining of nonmetallic minerals and metallic minerals and is even more certain there should be no discrimination between talc and the other nonmetallic miner-

als. which have long had percentage depletion. We have no objection or argument against percentage depletion for other minerals; in fact, it is the only feasible means of permitting the producers a return of capital. Is there some reason why this method should be granted to coal, sulfur, and potash and not to talc?

[42] Statement of JOHN BISHOP, Chicago, Ill., representing the vermiculite interests:

[44] Vermiculite is the basic mineral from which the income of processors, fabricators, and dealers is derived. In this respect, it is comparable to iron, copper, or lead sold by mine owners or operators to furnaces and smelters. Just as the ores are sent to furnaces and smelters whose products are in turn sold to fabricators for the manufacture of countless articles of commerce, so vermiculite is sold to processors and fabricators to make therefrom a large variety of commercial products.

Basic metals such as iron, copper, and lead are permitted percentage depletion. Vermiculite occupies the same position in the nonmetallic industry. It should therefore be accorded the same depletion.

H. Rep. No. 802

(80th Cong., 1st Sess. (1947-2 Cum. Bull. 353))

[1] GENERAL STATEMENT

The purpose of this bill is to provide for the termination of a number of war and emergency statutory provisions related to internal revenue and customs. The bill also makes amendments to the Internal Rev-

enue Code appropriate in connection with the termination of certain of the statutes.

#### INTERNAL REVENUES

[2] Percentage depletion was allowed certain minerals during the war period. The minerals affected are ball and sagger clay, fluorspar, and rock asphalt provided for under the Revenue Act of 1942, and barite, beryl, feldspar, flake graphite, mica, lepidolite, spodumene, talc, and vermiculite provided for under the Revenue Act of 1943. These allowances were terminated with respect to taxable years beginning after December 31, 1946, the date proclaimed by the President as the date of termination of hostilities in World War II.

Your committee, after hearings on the subject, is of the opinion that such allowances should be continued for taxable years beginning after December 31, 1946, and also that percentage depletion should be allowed in the case of china clay, bentonite, gilsonite, and thenardite for taxable years beginning after December 31, 1946. Accordingly, the bill eliminates the existing provisions providing for such termination and allows percentage depletion for the four additional items last mentioned for the years specified.

#### [3] DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL.

#### [9] SECTION 15—PERCENTAGE DEPLETION

Section 15 by amendment to section 114 of the Internal Revenue Code and by repeal of section 124(e) of the Revenue Act of 1943 continues in effect, as permanent legislation, the wartime allowance of percentage depletion at the rate of 15 percent in the case of



the following minerals: Fluorspar, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene, barite, ball and sagger clay, and rock asphalt. Section 15 also adds china clay, bentonite, gilsonite, and thenardite.

Pursuant to the provisions of section 124(e) of the Revenue Act of 1943 and the President's proclamation of December 31, 1946, declaring hostilities in World War II terminated, the provisions of section 114 of the code regarding percentage depletion as to the items named above (except china clay, bentonite, gilsonite, and thenardite) ceased to be applicable with respect to taxable years beginning after December 31, 1946. Section 15 repeals section 124(e) of the Revenue Act of 1943 as of the date of its enactment and further provides that the amendments made to section 114 of the code shall be applicable with respect to taxable years beginning after December 31, 1946. The effect of this is that the percentage depletion rules as to the minerals named in existing law continue without change, and percentage depletion is allowable in the case of china clay, bentonite, gilsonite, and thenardite for taxable years beginning after December 31, 1946.

House Debate, 1947

(93 Cong. Record (Part 8), 80th Cong., 1st Sess.)  
(1947)

[9626] TERMINATING CERTAIN TAX PROVISIONS

Mr. KNUTSON. Mr. Speaker, I move to suspend the rules and pass the bill (H.R. 4069) to terminate certain tax provisions before the end of World War II.

The Clerk read as follows:

[9627]

## SEC. 15. Percentage Depletion

Mr. KNUTSON. \* \* \*

[9628]

On the question of percentage depletion allowances, the committee considered this subject in detail. Public hearings were held, at which both sides of the question had full opportunity to present their views.

Each of these products, including those added to the list by H.R. 4069 is an essential *raw material* badly needed in times of peace as well as in time of war. The products added by H.R. 4069 are ball and sagger clay, china clay, or Kaolin, bentonite, gilsonite and thenardite, or sodium sulphate. [Italics supplied.]

These products were added because the mining problems involved are similar and in some cases identical with the problems faced by producers of petroleum, coal, and minerals. The deposits of the new products added by the bill are known in some cases, but unknown in others. Yet the producers must constantly explore new fields to determine their commercial value or the existence of new deposits. The depletion allowance encourages this explorative work. It is an expensive process, Mr. Speaker, and one that cannot be avoided. Unless we make a proper tax adjustment in the case of these mining operations we will discourage, if not prevent, discovery of new sources. Obviously, we cannot afford to do that.

(80th Cong., 1st Sess., to accompany H.R. 4069 (1947-2 Cum. Bull. 359))

[1]

The Committee on Finance, to whom was referred the bill (H.R. 4609) to terminate certain tax provisions before the end of World War II, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

With the exception of committee amendments to sections 5, 7, 8, and 15, of the bill, and the addition by your committee of a section 16 to the bill, the bill is the same as passed by the House. The report of the Committee on Ways and Means on the bill is attached hereto as appendix A. A detailed explanation of the bill (which, except with respect to the committee amendments, is equally applicable to the bill as reported by your committee) is included in the House report.

[2]

Section 15 of the House bill provided that the war-time provision for percentage depletion in the case of certain minerals should be continued as permanent legislation, and further provided for percentage depletion in the case of china clay, bentonite, gilsonite, and thenardite for taxable years beginning after December 31, 1946. Your committee amendment to this section of the bill adds pyrophyllite and trona to the list of minerals for which percentage depletion is allowable for taxable years beginning after December 31, 1946.

## H. Conference Rep. No. 1097

80th Cong., 1st Sess. (July 25, 1947) (1947-2 Cum.  
Bull. 360)

[2] STATEMENT OF THE MANAGERS ON THE PART  
OF THE HOUSE:

[3]

Amendment No. 10: This amendment provides for percentage depletion at the rate of 15 percent in the case of bauxite for taxable years beginning after December 31, 1946. The House recedes.

Amendment No. 11: This amendment provides for percentage depletion at the rate of 15 percent in the case of pyrophyllite for taxable years beginning after December 31, 1946. The House recedes.

Amendment No. 12: This amendment provides for percentage depletion at the rate of 15 percent in the case of phosphate rock for taxable years beginning after December 31, 1946. The House recedes.

Amendment No. 13: This amendment provides for percentage depletion at the rate of 15 percent in the case of trona for taxable years beginning after December 31, 1946. The House recedes.

Amendment No. 14: This amendment provides, with respect to percentage depletion, that—

In the case of potash and thenardite, whether extracted from a mine or from a brine or other deposit, there shall be included in gross and net income from the property the income from other minerals or mineral salts extracted therefrom.

The Senate recedes.

Act of August 8, 1947

(c. 515, 61 Stat. 917, 919)

## SEC. 15. PERCENTAGE DEPLETION.

(a) Section 124(e) of the Revenue Act of 1943 (relating to termination of percentage depletion for certain minerals) is repealed as of the date of its enactment.

(b) So much of section 114(b)(4) of the Internal Revenue Code (relating to percentage depletion for certain minerals) as precedes the second sentence thereof, is amended to read as follows:

(4) *Percentage Depletion for Coal, Bauxite, Fluorspar, Flake Graphite, Vermiculite, Beryl, Feldspar, Mica, Talc (Including Pyrophyllite), Lepidolite, Spodumene, Barite, Ball, Sagger, and China Clay, Rock Asphalt, Phosphate Rock, Trona, Bentonite, Gilsonite, Thenardite, and Metal Mines, Potash, and Sulfur.*—

(A) *In General.*—The allowance for depletion under section 23(m) shall be, in the case of coal mines, 5 per centum, in the case of metal mines, bauxite, fluorspar, flake graphite, vermiculite, beryl, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, ball, sagger, and china clay, phosphate rock, rock-asphalt mines, trona, bentonite, gilsonite, thenardite (from brines or mixtures of brine), and potash mines or deposits, 15 per centum, and in the case of sulfur mines or deposits, 23 per centum, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property.

(c) The first sentence of section 114(b)(2) of the Internal Revenue Code (relating to discovery value) is amended to read as follows:

In the case of mines (other than metal, bauxite, coal, fluorspar, flake graphite, vermiculite,



beryl, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, potash, ball, sagger, and china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite, thenardite, or sulfur mines) discovered by the taxpayer after February 28, 1913, the basis for depletion shall be the fair market value of the property at the date of discovery or within thirty days thereafter, if such mines were not acquired as the result of purchase of a proven tract or lease, and if the fair market value of the property is materially disproportionate to the cost.

(d) The amendments made by subsections (b) and (c) of this section shall be applicable with respect to taxable years beginning after December 31, 1946.

1947-1948

[In hearings the mining industry recommended clarification of the definition of *net* income from the property, but no action was taken by Congress.]

*House Hearings, 1947*

(Revenue Revisions, 1947-48, Hearings before the Committee on Ways and Means, House of Representatives, 80th Cong., 1st Sess. (1947))

¶ [Part 3]

[1855] Statement on behalf of the mining industry presented to the Committee on Ways and Means of the House of Representatives by H. B. FERNALD, chairman, tax committee, and JULIAN D. CONOVER, secretary, American Mining Congress, July 1947:

The following statement is presented by the tax committee of the American Mining Congress to set forth its recommendations for certain changes which should be made in the Revenue Code in the interest of fair and equitable treatment of the mining industry.

Certain of these recommendations relate to problems peculiar to the mining industry, while others are with respect to matters of great importance to the mining industry but which also affect other industries.

[1856] A. SPECIAL MINING PROBLEMS

Under this division we present certain matters which relate particularly to mining. The essence of mining is that its current operations necessarily represent a continual realization upon its capital assets. It realizes its gains only as it depletes its capital reserves. Its sales necessarily involve the sale of capital assets. Our tax laws have generally recognized the principle that a gain realized on the disposition of capital assets should be taxed at a lower rate than may be applied to recurring ordinary income. This principle is directly recognized in realization upon timber. For mining, we have over a long series of years worked out a different plan which allows, as an annual deduction, depletion based on cost (or on March 1, 1913 value), discovery depletion and percentage depletion. These provisions have repeatedly been considered at great length by Congress, and each time Congress has been satisfied that the present plan gives no more than a reasonable allowance for depletion for the mining industry.

We therefore urge that present depletion provisions not be changed in any way which would make them less favorable to the mining industry.

[1857] On the other hand, there are many problems connected with the mining industry and its depletion which need better and clearer statement in the law, to simplify and make more certain the interpretations involved, and to prevent abstruse and difficult prob-

lems and computations which under the Bureau's administration are now being raised. *We believe there are none of our recommendations which depart from the original intent of these provisions or from the Bureau's practice of earlier years.* [Italics supplied.]

We accordingly present the following recommendations regarding special mining problems:

1. *Definition of "net income from the property" for purpose of percentage depletion.*

There is need for writing into the law a definition of "net income from the property" as that phrase is used in section 114(b)(4) of the code, which imposes the limitation that percentage depletion for mines "shall not exceed 50 percentum of the net income of the taxpayer (computed without allowance for depletion) from the property \* \* \*." The provisions of the law relating to percentage depletion of mines, as first enacted in 1932 and subsequently reenacted without change in this regard, have not defined this wording. It was first defined in regulations 77, article 221 (h) which definition, substantially unchanged, has been continued through subsequent regulations and is section 29.23(m)-1(g) of regulations 111. It is believed that the original regulations were intended fairly to express the congressional intent, but administrative practices within the Bureau have gradually developed to reduce the amount of "net income from the property" below the amount which under earlier practices was considered allowable. The courts have generally tended to support administrative determinations where the law is not definite in prescribing its basis. To make clear the intent of Congress and give the taxpayer protection, it seems necessary that the law should adequately define this phrase.

\* \* \* \* \*

The proposed definition is intended to simplify the computations and limit the deductions to those items which have a direct bearing upon the production of income from the particular property on which the percentage depletion is allowable.

We accordingly recommend the following amendment:

Add to section 114(b)(4) a new subparagraph, (C), as follows:

“(C) Definition of Net Income from the Property—As used in this paragraph the term ‘net income from the property’ means the gross income from the minerals from the property, less the allowable deductions directly attributable to the mineral property upon which the depletion is claimed and *the allowable deductions directly attributable to the processes listed in paragraph (B) of this subsection insofar as they relate to the products of such property*, including operating expenses, development costs properly chargeable to expense, depreciation, property taxes, losses sustained, etc., but excluding any allowance for depletion. Such expenses or deductions shall not include expenses or deductions attributable to, or arising out of expenditures on, other property or assets, irrespective of whether such property or assets are income producing or active. Deductions not attributable to, or arising out of particular properties, processes or assets, such as general [1858] overhead, shall be fairly allocated to all properties, processes, and assets whether active or inactive. The term ‘general overhead’ as used herein shall be deemed to mean the overhead relating to the property but shall exclude deductions and expenses of financial overhead of the taxpayer such as interest, taxes based on or measured by income, capital stock taxes, and the like. If more than one active mineral property is involved, the de-

ductions apportioned to the mineral extraction in the processes listed in paragraph (B) of this subsection shall in turn be fairly apportioned to the several properties, taking into account their relative production." [Italics supplied.]

This amendment, as an expression of congressional intent, should be given retroactive effect.

[Part 5]:

[3281]

Statement of L. H. PARKER on behalf of the Special Committee on Taxation, National Coal Association, Washington, D.C.:

Mr. PARKER. \* \* \*

[3282]

Thank you, Mr. Chairman, and I file this statement for the record.

Mr. WOODRUFF. That will be included as a part of your remarks, Mr. Parker.

(The statement referred to is as follows:)

Technical Amendments to the Internal Revenue Code Suggested by the Special Committee on Taxation, National Coal Association, Washington, D.C.

There are submitted herewith three suggested amendments to the Internal Revenue Code, with explanations. It is believed all of these amendments clarify existing law.

The first suggestion is that a definition of net income from the property be included in the code. Such a definition is now lacking.



1949

[The Technical Changes Act of 1949, c. 720, 63 Stat. 891, did not amend existing law relating to percentage depletion, but an amendment passed by the Senate would have extended percentage depletion to several additional minerals. The Congressional reports, together with a brief excerpt from the Senate debate, follow.]

S. Rep. No. 831

(81st Cong., 1st Sess. (1949-2 Cum. Bull. 289))

\* \* \* \* \*

[9] 9. *Percentage depletion for perlite and diatomaceous earth.*

Section 9, which was not contained in the House bill, amends section 114(b) of the Internal Revenue Code to provide a different basis for allowance of depletion in the case of mines or deposits of perlite and diatomaceous earth. The effect of the amendments made by this section of the bill is to add mines or deposits of perlite and diatomaceous earth to the list of non-metallic mines or deposits which are allowed depletion in the amount of 15 percent of the gross income derived therefrom, and to make inapplicable to these mines or deposits the allowance of depletion upon the basis of discovery value. It is proposed to allow percentage depletion only with respect to perlite and diatomaceous earth in the dried crude mineral form, before grinding or any other preparation for any particular market. Perlite is a volcanic glass, and diatomaceous earth, a chalk-like, or clay-like material which is the silicified skeleton remains of colonial algae.

The Director of the Bureau of Mines reports that although the Bureau does not have a detailed statistical record which would completely define the degree of competition of these minerals with those now accorded

percentage depletion, "such competition is known to exist." He further reports:

For example, diatomaceous earth is used as a heat-insulating material and as such competes with vermiculite in some applications. Diatomaceous earth is also used as a filler in a wide variety of products, and therefore competes in varying degree with other minerals that serve this market, such as china clay, bentonite, talc, and barite, all of which are allowed percentage depletion.

[10] Similarly, perlite competes with vermiculite in the lightweight aggregate market.

Other reports indicate that perlite or diatomaceous earth, or both are also competitive with ball and sagger clay, feldspar, mica, and pyrophyllite. Since all of these minerals, as well as those mentioned above by the Director of Mines, receive percentage depletion, your committee believes that the benefits of percentage depletion should also be extended to perlite and diatomaceous earth to remove any tax differential which might prevent them from competing on an equal basis with these other minerals.

*It is not proposed to allow percentage depletion with respect to the value added as the result of grinding or other special preparation because many of the extractors do not themselves carry on this process, but rather sell these minerals in crude form and let others carry on any processing required. Thus to allow percentage depletion with respect to this added value would discriminate against those selling these minerals in crude form, since percentage depletion is not allowable to processors. [Italics supplied.]*

The amendments made by this section are applicable with respect to taxable years beginning after December 31, 1948.

(95 Cong. Record (Part 10); 81st Cong., 1st Sess.)

[12995] Mr. CHAPMAN. Mr. President, on behalf of the Senator from Pennsylvania [Mr. Martin] and myself, I ask unanimous consent that there may be included in the Record, immediately following the adoption of the percentage-depletion amendment, a brief memorandum in which are stated various reasons why *refractory clays and quartzite* should be granted percentage depletion under section 114(b) of the Internal Revenue Code. [Italics supplied.]

There being no objection, the statement was ordered to be printed in the Record, as follows:

H. Conference Rep. No. 1412

(81st Cong., 1st Sess. (1949) (1949-2 Cum. Bull 295))

[5]

STATEMENT OF THE MANAGERS ON THE PART OF  
THE HOUSE

[11] Amendment No. 8. The Senate amendment added a new section percentage depletion at the rate of 15 percent in the case of perlite, diatomaceous earth, tripoli, granite, marble, borax mines and deposits, sand, gravel, stone, calcium and magnesium carbonates, and all other nonmetallic clays and minerals. The conferees agreed to eliminate this amendment with the understanding that the entire matter of percentage depletion will be considered early next year after full study and hearings. The Senate recedes.

1950

[Representatives of numerous mining industries testified in extensive hearings urging (1) rejection of the Treasury's proposal to reduce the percentage depletion rates except on metals and (2) allowance of percentage depletion to additional non-metallies. To a large extent the testimony consisted of explanations of the mining, processes applied, and uses of the various minerals, the pertinent portions of which are omitted here but set forth in Part B of this Appendix. Action on the allowance of percentage depletion to additional minerals was ultimately postponed but an amendment was adopted regarding transportation from the point of extraction to the plant or mill where the ordinary treatment processes are applied. The hearings, reports, and amendment are set forth below in sequence.]

**House Hearings, 1950**

(Revenue Revision of 1950, Hearings before the Committee on Ways and Means, House of Representatives, 81st Cong., 2d Sess., (Vol. 1))

[7] STATEMENT OF HON. JOHN W. SNYDER, SECRETARY OF THE TREASURY

[17]

By arrangement with your committee, our staff has been working with the staff of the Joint Committee on Internal Revenue Taxation since last summer on developing legislative suggestions for eliminating loopholes. The recommendations in this area represent the product of this joint effort. Other loopholes are still under study and will be brought to the attention of your committee at some future time.

I should like to refer first to the special allowances for depletion.

### SPECIAL DEPLETION ALLOWANCES

[18]

Specifically it is proposed that percentage depletion for oil, gas, and sulfur be reduced to 15 percent of gross income and that percentage depletion for non-metallic minerals be reduced to 5 percent. The existing 15-percent rate for depletion allowed to the metals would be left unchanged.

[279]

Statement of B. A. Hardey, Shreveport, La.:

Mr. HARDEY. Mr. Chairman and gentlemen of the committee, my name is B. A. Hardey. I live in Shreveport, La., and I am an independent oil and gas producer. \* \* \* These connections over the years have given me an insight into the many problems confronting the producer of petroleum.

[282]

*It is significant that the special provisions which Congress has adopted apply to oil and gas production only, and not to refining, transportation, and distribution of petroleum, since the latter operations are comparable with the usual manufacturing and distribution activities in other lines of business. The provisions have been no more than adequate to attract into this business enough activity to provide reasonable quantities of oil for an expanding economy. \* \* \* [Italics supplied.]*



[310] Statement of J. RUTLEDGE HILL, Chairman,  
National Sand and Gravel Association, Dallas, Tex.;

[314]

Sand and gravel compete with materials which are presently accorded the benefit of percentage depletion at the rate of 15 percent of gross income, with an over-all ceiling of 50 percent of net income. Sand and gravel should be given percentage depletion at the same rate.

[315]

Mr. JENKINS. Very well. As I understand it, you speak for the sand and gravel industry all over the United States?

Mr. HILL. That is correct, sir.

[328]

Statement of CHARLES W. NIELSEN, treasurer,  
Edgar Bros. Co., Metuchen, N.J.:

Mr. NIELSEN. \* \* \*

It was our intention to have this presentation made by Mr. William B. S. Winans of Aiken, S.C., president of the Kaolin Clay Producers Association. Mr. Winans is ill, unfortunately, and has asked me to make this presentation in his behalf.

I am also representing certain kaolin, or china clay, producers who are not members of the Kaolin Clay Producers Association.

The whole purpose of my appearance is to urge the retention of percentage depletion in china-clay

mining—or kaolin clay mining—the terms are synonymous—and to urge that the 15-percent figure which the present law gives china clay be retained at that level.

[332] Statement of RALPH L. DICKEY, president, The Kelley Island Lime & Transport Co., Cleveland, Ohio:

Mr. DICKEY. My name is Ralph L. Dickey. I am president of the Kelley Island Lime & Transport Co. of Cleveland, Ohio. I am appearing as a representative of a committee of the National Lime Association requesting a 15-percent depletion allowance for limestone when calcined or when used by the metallurgical or chemical industry. \* \* \*

[335] Statement of Prof. KENNETH K. LANDES, chairman, Department of Geology, University of Michigan, Ann Arbor, Mich.:

One year ago I prepared for the National Lime Association a survey of domestic high-grade limestone deposits. This survey has been published by that association and distributed to your committee.

[348]

Statement of DONALD A. CALLAHAN, Wallace, Idaho, vice president, The American Mining Congress; also representing the Idaho Mining Association and the Northwest Mining Association:

Mr. CALLAHAN. My name is Donald A. Callahan. I live at Wallace, Idaho. I am appearing here representing the American Mining Congress as its vice president. I am also representing the Idaho Mining Association and the Northwest Mining Association,

which embraces operators in Washington, Oregon, western Montana, and northern Idaho.

[349]

Mr. CALLAHAN. I want to address myself particularly to the subject of percentage depletion and the rates for metal mines as set forth in the amendment to the revenue laws adopted in 1932. I also wish to address myself to the subject of depletion generally as applied to mines.

As the committee is well aware, the 1932 amendment provides for depletion allowance in the following language (reading):

The allowance for depletion shall be in the case of metal mines 15 percent \* \* \* of the gross income from the property during the taxable year.

This amendment was adopted following a report of the staff of the Joint Committee on Internal Revenue Taxation. Although this rate and the principle of percentage depletion generally has been attacked several times since then, full hearings have been held, the Congress has seen fit to continue both the principle and the rate. \* \* \*

[351] \* \* \* *The miner does not expect the Government to guarantee a profit to him.* He expects to pay fair taxes, but he must have at least the hope that if there are profits they will be subject only to a fair tax upon true income. The constant threat of reduction or complete elimination of depletion allowances is a deterrent to investment of risk capital and in consequence to the discovery and development of new ore bodies. [Italics supplied.]

[352]

I should also like to submit for the record a memorandum on depletion of mines and also a statement on mining taxation by the American Mining Congress, which I should like to submit with the request that it be inserted in the record at this point.

(The documents referred to follow:)

DEPLETION OF MINES—A STATEMENT BY THE  
MINING INDUSTRY

(American Mining Congress, Washington, D.C.,  
February 1950)

1. *The nature of mining as distinguished from other industrial enterprises:*

To understand the problems of depletion it is necessary to have some knowledge of what is involved in *extracting minerals from the earth, processing them, and delivering the metal product to the fabricators* to be fashioned into the machines and articles so essential to our modern way of life. [Italics supplied.]

[354]

3. *Depletion is a return to the mining industry of the capital consumed in its operations:*

The mineral in place in the ground is the principal capital of every mineral producer. As each ton is extracted, a certain portion of his capital is actually consumed. A portion of his proceeds from each ton is the return of his capital, and only a portion is income. Since the inception of the income tax, every effort has been made to tax income only, and to avoid taxing capital. Depletion is merely the method by which the return of capital is computed. The right to a

return of capital has always been recognized. This right has never been seriously questioned.

[355]

4. *The present system of computing depletion resulted from careful study and affords the best means for determining the annual consumption of capital:*

After years of experience with other methods of computing depletion, the Congress in 1932 included the present percentage method for metal mining, coal, and sulfur. This was upon the recommendation of the staff of the Joint Committee on Internal Revenue Taxation, which made an exhaustive study of the subject. The joint committee held extensive hearings, and the printed reports of the staff of the joint committee and of the hearings before the committee were considered by the Congress in the adoption of the percentage method and in fixing the rates. The rates so fixed were lower than the average rates actually allowed under the previous laws. Percentage depletion has subsequently been extended to certain other minerals, and the rates on these are among the rates subject to present criticism.

The following is quoted from the letter of Mr. L. H. Parker, chief of Staff to the Joint Committee on Internal Revenue Taxation, transmitting the report to the staff of that committee, dated December 17, 1929:

*The report of the staff of the joint committee called special attention to the uncertainty and lack of uniformity under the methods of computing depletion which theretofore had been the only methods allowed. Tables were given showing the wide difference in allowances of depletion between different branches of the industry and individual taxpayers. The inclusion*



of the percentage method has remedied this situation. [Italics supplied.]

One of the objects sought to be attained by the percentage method was the elimination of the inequality which had existed as between competing members of the mining industry. Under the methods in use prior to 1932, certain companies had been able to establish adequate depletion allowances which, by reason particularly of the geological nature of their deposits, were not available under the statute to others. The present laws tends to remove this inequality and to give all mining taxpayers some measure of protection against taxation of their capital. [Italics supplied.]

The small-mine operator cannot afford to spend the money necessary to establish the value of his mineral deposits and the corresponding depletion value of his unit of production. Percentage depletion removes the necessity for such expenditures. It provides a simple, understandable method by which, from the inception of his enterprise, he may receive the reasonable allowance for depletion contemplated by the statute. It assures him fair and equal treatment with other operators. It protects him against the taxation of the capital he has consumed in his operation. [Italics supplied.]

#### Conclusion

[356] The principle of percentage depletion is fair and equitable, and the existing rates are not excessive. Percentage depletion permits substantial savings to both Government and taxpayer in the establishment of a basis for depletion allowances; it protects the small taxpayer against discrimination and against excessive taxation of his capital; it does not return

to the mining industry as a whole more than the annual consumption of its capital value; and *it constitutes the simplest and best procedure yet devised for sustaining capital investment* in an industry that is vital to the welfare and security of our country. [Italics supplied.]

[377]

Statement of CHARLES F. WILLIS, Phoenix, Ariz., secretary, Arizona Small Mine Operators Association:

Mr. WILLIS. The name is Charles F. Willis, of Phoenix, Ariz. I am secretary of the Arizona Small Mine Operators Association and a member of the Tax Committee of the National Minerals Advisory Council to the Department of the Interior. The Arizona Small Mine Operators Association is an organization of approximately 3,800 members who are interested in an opportunity of developing the mineral resources of the State of Arizona.

[379]

We, in Arizona, are not alone concerned with the metal-mining tax situation, but we are also interested in the proposal for the nonmetallics. We have potential resources of important nonmetallics, but their problem is not only one of applying venture capital and determining what they have. The major problem in many nonmetallics is the developing of a marketable product and creating of a market for the same. This angle often requires a greater application of skill and capital than is indicated by the value of the body of mineralized material. It has only been through the developing of a market that any value has

been created in the rock. *Yet, it is only on the value of the rock in place that depletion allowances are given, and that is proposed to be cut. There is less and less incentive to create this new wealth. [Italics supplied.]*

[380]

Statement of KENNETH B. RAY, counsel for Food Machinery & Chemical Corp., and also representing Phosphate Rock Industry Group:

[381]

At the time trona was given the right to percentage depletion the company understood that it was the fixed policy of Congress to continue the percentage-depletion allowance for trona at the 15-percent rate for the reason that the metal-mining industries had enjoyed such a rate for an extended period of time. The statements made in the congressional debates confirm this understanding. \* \* \*

[382]

All of the reasons which were presented by the industry in 1947 for adding trona to the minerals entitled to percentage depletion remain true today. Among other considerations it was pointed out then that trona is comparable to metal mining and that it would be at a competitive disadvantage if forced to compete with metal mining companies that now enjoy the benefits of percentage depletion.

In 1947 the benefits of percentage depletion were also extended to phosphate deposits. This turned out

to be a particularly wise piece of legislation since the Government for many years had been endeavoring to secure widespread development of the phosphate deposits of southeastern Idaho. Following the addition of phosphates to the statute this company has expended over \$10,000,000 in an electric furnace project to utilize the Idaho phosphate deposits. The economics of this development are based on *percentage depletion for the basic raw material, phosphate rock.*

\* \* \* [Italics supplied]

[383] The CHAIRMAN. We thank you.

Mr. JENKINS. I ask unanimous consent that Mr. Douglas Whittlock, of Washington, D.C., be permitted to present a brief. He represents the structural clay products industry.

The CHAIRMAN. Without objection it is so ordered.

(The brief referred was not received in time for inclusion in the record.)

Statement of FRED O. DAVIS, vice president and treasurer, Potash Co. of America, Carlsbad, N. Mex.:

It is only a few years since representatives of the American potash industry appeared before both the Ways and Means Committee in the House of Representatives and the Finance Committee of the Senate. At that time potash was brought within the percentage depletion provisions of the revenue act and was granted such depletion on a permanent basis.

During the consideration of the Revenue Act of 1943, when percentage depletion on a permanent basis was granted to potash, a comprehensive statement with reference to the foregoing points was sub-

mitted and since that time and during the period when percentage depletion has been in effect, the following developments have occurred:

[368] Mr. LYNCH. What is the price of potash f.o.b. mines?

Mr. DAVIS. The crude product is worth about \$4.50 per ton of ore. The refined product, which takes 2½ tons to produce, is about \$20 per ton.

[413] Statement of JOHN H. BISHOP, Chicago, Ill., representing Miners of Vermiculite:

(The prepared statement of Mr. BISHOP follows:)

[414]

Vermiculite is a *basic mineral which is sold in its crude or concentrated form to processors* who exfoliate it and from the processed mineral fabricate many different types of materials, all of which are sold through dealers. The income from the industry, therefore, is derived from three sources: the miners, the processors, and the dealers: [Italics supplied.]

Vermiculite ore in its concentrated form sells for approximately \$10 per ton. Exfoliated vermiculite that is sold by processors brings approximately \$75 per ton. \* \* \*

[431] Statement of S. W. TUTTLE, Vice President and Secretary, International Talc Co., Inc., New York, N.Y.:

I would like to describe briefly the operations engaged in by my company and by other talc companies



which influenced the Congress to grant us this depletion allowance. \* \* \*

[441] Statement of E. A. GARBER, president, Harbison-Walker Refractories Corp., Pittsburgh, Pa.:

Mr. GARBER. I not only represent Harbison-Walker but over 50 refractories who produce about 90 per cent of the refractory or fire material used in the United States. Next to agriculture, we probably are the second basic industry in the United States. Our products are used in every phase of industry where heat resistance is necessary.

[464] Statement of JAMES W. HALEY, secretary and general counsel, National Coal Association, Washington, D.C.:

[466] For the record and for the consideration of the committee, I attach to my statement five amendments of a technical nature calculated to remove from doubt some of the fields of disagreement arising between the coal industry and the Bureau of Internal Revenue. A brief description of the amendments follows.

Appendix No. 1 sets forth the language of a proposed amendment calculated to correct the tendency on the part of the Bureau of Internal Revenue to exclude from computations for purposes of percentage depletion essential elements of cost involved in transporting coal *from the place of extraction to the tipple or preparation plant*. This question is actively before the Bureau at this time and involves many coal operator taxpayers. We think the law is clearly in

our favor as it now stands, but the Bureau does not seem to think so. (*Italics supplied.*)

[468]

### APPENDIX No. 3

Definition of "net Income from the Property"—Amendment to Section 114(b)(4)—Internal Revenue Code.

Section 114(b)(4) is amended by adding at the end thereof a new subparagraph (C) to read as follows:

"(C) Definition of Net Income from the Property.—As used in this paragraph the term 'net income from the property' means the 'gross income from the minerals from the property' as defined in subparagraph (B) of this subsection, less \* \* \* [*Italics supplied.*]

[470] Statement of Hon. HARRY P. O'NEILL, a Representative in Congress from the State of Pennsylvania:

MOFFAT COAL Co.,  
SCRANTON 2, PA., *February 7, 1950.*

HON. HARRY P. O'NEILL,  
*Representative, Tenth District,*  
*House Office Building, Washington, D.C.*

DEAR MR. O'NEILL: Recently, in his tax message, the President commented on percentage depletion as applied to the mining industry and advocated the elimination of this provision of the current revenue act.

[471] The allowance of percentage depletion under the present law was carefully and fairly set by experience; and the percentage method affords a *simple*

*and equitable* means of computing the reasonable allowance for the exhaustion of the mineral deposit which has always been contemplated in the law. \* \* \*  
[Italics supplied.]

Statement of W. P. HAMBLÉN, Houston, Tex.:

Mr. HAMBLÉN. Mr. Chairman and gentlemen of the committee, I am W. P. Hamblén, of Houston, Tex. I am appearing on behalf of a number of companies engaged in the production of mineral shell deposits. I am a director and an attorney for the W. D. Haden Co., of Houston, Tex., one of the larger producers of mineral shell in the State of Texas.

[480] Statement of RUSSELL RAREY, president, Marble Cliff Quarry Co., Columbus, Ohio:

Mr. RAREY. I would like to have about 5 minutes, if I may. We operate a limestone open quarry near Columbus, Ohio, and in the western part of the State a limestone underground mine. \* \* \*

[481] As a member of the executive committee and of the percentage depletion committee of the National Crushed Stone Association, I have been authorized, along with Mr. Krause, to present a statement on behalf of the National Crushed Stone Association, and the Agricultural Limestone Institute.

[483] We heartily favor the percentage depletion method for other mining industries, but the crushed-stone industry fails to see any essential difference between the mining of crushed stone and certain non-metallic minerals and is convinced that the discrimination between crushed stone and other nonmetallic minerals which have long had percentage depletion should be eliminated.

[489] Statement of HORACE C. KRAUSE, president, Columbia Quarry Co., St. Louis, Mo.:

Mr. KRAUSE. My name is Horace C. Krause, President of the Columbia Quarry Co. I am chairman of the percentage depletion committee for the National Crushed Stone Association and Agricultural Limestone Institute.

[491] Statement of HENRY MULRYAN, Glendale, CALIF.:

At the present time I am the executive vice president and general manager of the Sierra Talc & Clay Co., which company operates 14 mines in the States of California, Nevada, New Mexico, and Montana.

[492] You have heard a great deal about the percentage depletion. I would just like to make this remark, why the rates should be 15 percent. The rate for talc should be the same as that allowed metal mines. The mining, milling, and processing of talc is comparable to metal mining and in many instances requires more complex and costly operations. \* \* \*

H. Rep. No. 2319

(81st Cong., 2d Sess. (1950-2 Cum. Bull. 380))

[64]

#### (F) PERCENTAGE DEPLETION

At your committee's hearings on this bill a number of witnesses pointed out that the depletion provisions of existing law discriminate against the producers of

certain nonmetallic minerals, including coal. Existing law permits depletion based on cost to all the mining industries, but allows percentage depletion to oil, gas, sulfur, metal mines, and certain enumerated nonmetallic minerals, if this produces a larger deduction. The rate allowed in the case of coal is 5 percent of gross income. The other enumerated nonmetallic minerals other than sulfur receive 15 percent, which is also the rate allowed to metal mines.

The testimony before your committee revealed that in a number of cases nonmetallic minerals which are not enumerated in existing law are competitive with the minerals receiving percentage depletion or have just as good a claim for such treatment as the enumerated minerals. The testimony received by your committee indicated also that the 5 percent rate allowed in the case of coal is of little practical value, and that the coal-mining industry is peculiarly in need of more favorable tax treatment because of the inroads on its potential markets by alternative sources of energy, particularly oil and gas.

Section 204 of your committee's bill adds to the list of nonmetallic minerals which may elect percentage depletion at a 15 percent rate, borax, fuller's earth, refractory and fire clay, quartzite, perlite, [65] diatomaceous earth, metallurgical and chemical grade limestone, and tripoli. Existing law allows the 15-percent rate to thenardite, but only when it is obtained from brines, or mixtures of brine. This restriction is removed by your committee's bill.

The bill increases the percentage allowed in the case of coal from 5 to 10 percent, and sets up a new group of minerals to which percentage depletion is available at the rate of 5 percent. This group consists of sand, gravel, granite, marble, stone, brick and tile clay, shale and shell.



The rates used under the percentage depletion option are, of course, applied to the gross income from the property. In order to restrict depletion to the actual product of mineral extraction, it is stipulated in your committee's bill that the gross income to which the percentage depletion rate is to be applied shall not include income resulting from the transportation of the product beyond the property.

It is estimated that these changes in the percentage depletion allowance will reduce the revenues by about \$35 million a year when fully effective.

House Debate, 1950

(96 Cong. Record (Part 7) 81st Cong., 2d Sess.)

[9282]

\* \* \*  
 Mr. CASE of South Dakota. My attention has been called to the fact that under section 204, having to do with percentage depletion, the bill proposes to add a clause to the existing law on gross income from mining in the following words: "but such term shall in no case include transportation beyond the property."

In connection with nonmetallic minerals, such as feldspar and bentonite, and other minerals of that sort, the common practice is to collect or pick up the rough ores and then transport them to a central mill. In many cases 50 percent or more of the cost of the operation is involved in getting them to the processing plant. Until these ores have been processed, they are not usable. You have only crude ores. They are not products. They are only moved rocks or clays. *The transportation to a processing mill, whether 100 yards or 20 miles, is a part of the mining. Transportation after milling or even grinding is something else. To make this clear, would the chairman say that it is not intended to deny the transportation costs where they*

*are a part of the handling of the crude ore before it is processed or milled?* [Italics supplied.]

Mr. DOUGHTON. The subject of depletion was one of the controversial subjects that was before our committee and was considered very carefully. What we did is the decision of the majority members of the committee.

I yield to the gentleman from Tennessee [Mr. COOPER] if he has some observation to make.

The CHAIRMAN. The time of the gentleman from North Carolina has again expired.

Mr. DOUGHTON. I yield myself four additional minutes.

Mr. COOPER. Mr. Chairman, I am sure the chairman will bear in mind, and if the gentleman from South Dakota [Mr. CASE] will refer to page 65 of the report, he will see the explanation of this provision. Briefly, it simply means this, that percentage depletion is provided for the production of the mineral but not for the transportation of it.

Mr. CASE of South Dakota. On page 65 the language says, "transportation of the product." If "the product" means the milled mineral, that is one thing, but if it is the crude ore, that is something else.

Mr. COOPER. Well, it is crude ore that is being talked about.

Mr. JENKINS. Mr. Chairman, will the gentleman yield to me?

Mr. DOUGHTON. I yield.

Mr. JENKINS. I would like to call attention to this proposition: Just as the gentleman from South Dakota says, there has been a great deal of complaint lately with reference to that language. I participated rather actively in this matter in the committee. We discussed this proposition, which is the mining of coal, and it was decided that in coal production there is a

lot of expense before the coal finally leaves the property on which it is mined. Sometimes it is screened, and sometimes it is washed and pulverized and made into different sizes. At that time, while we were discussing this, we intended that all that expense would be included, before taking the coal further. As an illustration, in Ohio, for instance, we have what we call strip mines. The coal is mined and taken long distances before it is disposed of. It is not treated at all. It is taken up as far as Detroit, for instance, and sold. It would not be fair to consider that transportation as a part of the depletion cost, because that is simply going too far.

Mr. CASE of South Dakota. But coal is a usable product when it is mined, generally speaking; whereas, clays are not.

Mr. JENKINS. With reference to the production of clay, in most of the countries where clay is produced the brick and clay plants are close by, contiguous to where the clay is produced, but in some places they are not. In some places the clay must be hauled long distances. If that is the case, the same applies as with reference to coal. I doubt whether the language we have does fix it definitely and closely enough. This ought to be made more specific when the bill goes to the other body. But the intention was to grant to those people who produced minerals a rather complete concession, but it was not intended to apply to that product every step they hauled it.

Mr. CASE of South Dakota. If the haulage is merely a matter of 5 or 6 or 12 or even 20 miles to a central milling plant, it seems to me it is a part of the cost of production, because the product is not usable until it leaves the mill.

Mr. JENKINS. That will be a proposition of interpretation by regulation or further clarification in the other body.

Senate Hearings, 1950

(Revenue Revisions of 1950, Hearings before the Committee on Finance, United States Senate, 81st Cong., 2d Sess., on H.R. 8920).

[299] Statement of M. D. HARBAUGH, vice president, Lake Superior Iron Ore Association, Cleveland, Ohio.

Mr. HARBAUGH. Mr. Chairman and members of the committee, my name is M. D. Harbaugh. I am vice president of the Lake Superior Iron Ore Association of Cleveland, representing most of the companies that mine and ship iron ore from the important Lake Superior district of Minnesota, Michigan and Wisconsin.

[301]

Section 204(c) of the bill, regarding percentage depletion, in revising the definition of gross income from mining, would create a deterrent that certainly will adversely affect the development of low-grade ores including the taconites, which require beneficiation. Plants cannot always be established directly at the property but must be located at the nearest practical point as determined by physical conditions and other factors. The transportation is an integral part of the whole operation of mining and beneficiation. Disallowance of transportation in computing gross income for depletion, would impose a severe handicap to the industry's program for developing these low-grade deposits.

Senator MILLIKIN. How far would you carry the transportation cost?

Mr. HARBAUGH. Well, we have plants that are located several miles from the source of the ore, centralized plants which are necessarily large in which ores from numerous small pits or small workings can be treated.

Senator MILLIKIN. How do you treat the iron ore at those smaller plants?

Mr. HARBAUGH. The ore is treated in these plants by washing to remove some of the impurities and by other concentration processes such as are technically known as jigging and heavy density separation.

Senator MILLIKIN. You are simply preparing the ores for the plant?

Mr. HARBAUGH. Yes, sir. *This part that is treated would not be marketable without this treatment.* [Italics supplied.]

Senator MILLIKIN. You would not run your cost down to Pittsburgh?

Mr. HARBAUGH. No. *This involves the transportation to the processing plant where we make the first marketable product.* [Italics supplied.]

Senator TAFT. And a product which can be shipped on boats?

Mr. HARBAUGH. Which can be shipped on boats and which is usable in the premises.

The CHAIRMAN. Was it not intended by the House to exclude the transportation cost of the first processing plant?

Senator TAFT. These are the words:

\* \* \* *but such terms shall in no case include transportation beyond the property,*

That is what the House put in.

Mr. HARBAUGH. The whole problem is, what do you mean by "the property"? If the property is the



particular place from which the crude ore is taken, then that is a very restrictive clause because the processing plant may be a few miles away or it may be a mile away.

Senator MILLIKIN. You might have four separated properties owned by the same people who have a central processing plant and this language would be ridiculous in that case.

Mr. HARBAUGH. That is right and in the future in the treatment of this taconite that will be more important than now.

The CHAIRMAN. *Mr. Stam, would you be prepared to say whether the House intended by the use of this language to exclude the cost of first processing, the first step in the processing to render marketable or merchantable the minerals?* [Italics supplied.]

[302] Mr. STAM. I think when the problem came up before the House committee they were particularly concerned with the new minerals that had come in, such as sand and gravel and some of those, and it was pointed out that if you computed the depletion allowance on the sand at the pit and then you carried it 3 or 4 miles away in a truck, that the cost would be much greater. I mean that is the way the thing originally came up, but in discussing it the House decided that they would make the amendment effective for the existing depletion allowances as well as the new depletion allowances that were brought in. *So that I think the way the amendment was worded it was intended to put a limitation on the whole allowances but it started from the idea of sand and gravel and some of those minerals that they did not want to give a bigger allowance to than the value at the time it was taken out.* [Italics supplied.]

Senator TAFT. They do not propose to include

transportation on ships down to Pittsburgh, of course?

Mr. STAM. That is right.

Senator MILLIKIN. What is the answer to the argument, if there was an argument, that it is practical to limit it to the property? We were just discussing, Mr. Stam, that sometimes there will be three or four properties all served by a central cleaning-up plant. In coal mines you have a washing problem, I assume, similar to your problem?

Mr. HARBAUGH. Very similar.

Senator MILLIKIN. *In other words, you have no salable product until you get through that first processing business which does not change the character of the product. It merely renders the product marketable.* [Italics supplied.]

[447]

Statement of LOUIS H. HEYL, vice president and general manager, the Wyodak Chemical Co., Cleveland, Ohio:

We are miners and processors of bentonite clay. Under section 114(b) of the Internal Revenue Code, the mining and processing of bentonite clay is granted certain exemptions in the form of percentage depletion along with several other mineral products.

[448]

It is therefore a definitely established fact that trucking bentonite to the processing plants where it must be dried, granulated, or ground, is a vital portion of the processing steps necessary to develop it to its "first commercially marketable product" stage;

that is, in dried, ground, or granulated form and packed in bags. [Italics supplied.]

Senator MILLIKIN. *Your first step does not change the character of the deposit in any way?* [Italics supplied.]

Mr. HEYL. None whatever; it just reduces the moisture.

Senator MILLIKIN. That is, cleaning it up, drying it, and putting it into a certain form?

[449] Mr. HEYL. That is correct.

[757] Statement of JAMES W. HALEY, Southern Building, Washington, D.C., secretary of The Special Tax Committee, National Coal Association, accompanied by L. H. PARKER, Chairman.

My principle purpose in appearing before the committee today is to urge you to recommend that the Senate concur in the House action in raising the gross depletion for coal from 5 to 10 percent. I also deal with the necessity for clarifying the Internal Revenue Code [758] with respect to what constitutes gross income from the property for purposes of interpreting the depletion allowance and also with respect to corporate earnings and profits accumulated prior to March 1913.

[768]

Statement by HENRY B. FERNALD, chairman, tax committee, American Mining Congress:

[771]

(II) Section 204, percentage depletion: (1) We urge that you reject the Treasury recommendation

regarding percentage depletion, as the House has done after extended hearings. We believe it is unnecessary to repeat what was there presented to evidence that percentage depletion is no more than a proper allowance to the mining industry for capital exhaustion.

(3) Section 204(c) of the bill proposes to add the words "but such term shall in no case include transportation beyond the property" at the end of the second sentence of section 114(b)(4)(B), which, for determining gross income for percentage depletion purposes, defines the term "mining" to include both extraction from the ground and also "the ordinary treatment processes normally applied." The House committee report (p. 84) states that the proposed amendment "is merely declaratory of existing law." This statement is erroneous.

Section 114(b)(4)(B) of the code was written into the law in 1943, as stated in the report of the Committee on Finance (S. Rept. 627, 78th Cong., 1st sess., p. 23):

The purpose of the provision is to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation, and to give reasonable specification of what are to be considered such processes for various kinds or classes of mines.

The law has never contained such a definition, and its absence has given rise to numerous disputes. The definition here prescribed expresses the congressional intent of these provisions as first included in the law, and is in accord with the original regulations and the Bureau practices and procedures thereunder. It is therefore made retroactive to the date of such original provisions.

The first sentence of the definition in section 114(b) (4)(B) states that gross income from the property means the gross income from mining. The second sentence states that mining shall include not merely extraction of the ores but also the ordinary treatment processes normally applied. The third sentence specifies the ordinary treatment processes to be included for each of the several classifications there set forth as (i), (ii), (iii), and (iv). *The processes are stated in considerable detail, following the lines of the Treasury regulations prescribed under the 1932 act and continued for many years thereafter. Such regulations (for example, art. 23(m)-1(g); Regulations 101) were definite in stating that the gross income determination should be "before transportation from the place where the last of the processes listed below was applied." Transportation necessary to move the minerals to the plants where the ordinary treatment processes were performed was, like the processes themselves, to be considered as part of mining. Transportation from the place where the last of the specified processes was applied was not to be considered as part of mining; nor were any further processes beyond those specified. The processes specified gave the cut-off point between what was and what was not to be considered mining in each case. [Italics supplied.]*

We are confident that Congress, in adopting the 1943 amendment to express the intent of the prior law, intended that the definition of "gross income" written into the law should carry the same meaning and the same cut-off point with regard to transportation as had been set forth in the early regulations and had been followed in Bureau procedure. [Italics supplied.]

Sometimes plants for concentrating or other processes specified can be located directly on the mining



property. At other times terrain, necessary water supply, [772] or other factors may make that impossible, and a plant will be located at the nearest practical point at which the processes can be efficiently performed. This is normal mining procedure.

Lately there has been some disposition in the Bureau to raise questions in this regard which were not raised and would not have been admissible under the earlier regulations and procedures. For this reason, and because of the statement erroneously made in the House committee's report, we believe the intent of the law should be made clear by the following amendment in lieu of that proposed by section 204(c) of the bill:

(1) That the second sentence of section 114(b)(4) (B) should be amended to read as follows:

The term "mining" as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground, but also (a) the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products and (b) the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plant or mill in which the ordinary treatment processes are applied thereto.

It is understood that the amendment now proposed in section 204(c) of the bill was intended primarily to apply to sand, gravel, etc., for which percentage depletion is proposed to be newly allowed by section 114(b)(4)(A)(i). If none of the existing classifications (i) to (iv) in section 114(b)(4)(B) is deemed to give the satisfactory cut-off point for these newly included minerals, the appropriate method to make clear the basis for them would be by inserting in the third sentence of section 114(b)(4)(B) a new subdivision

(v) which would specify the processes, if any, which should be considered as the "ordinary treatment processes" with respect to such minerals.

In this way the present meaning of the law will be maintained and clarified at the same time that the appropriate specifications are set forth for the newly added minerals, in harmony with the structure of the section and with its specifications for other classes of minerals.

[778]

Senator MILLIKIN. *Will you give us some examples of the processing going on in normal operation when the ore comes out of the ground?* [Italics supplied.]

Mr. FERNALD. I will furnish that to you later if I may.

Senator KERR. With reference to the transportation, does this contemplate the reasonable ordinary cost of transportation from the mine to a mill located nearby or to what extent might that be expanded?

Mr. FERNALD. The kind of rule that we are asking for, sir, is to have it where the mill or processing plant is located at the nearest reasonable point for the efficient application of the processes, the transportation from the mine to that point.

Senator KERR. What might that involve?

Mr. FERNALD. That would depend a great deal on the question of terrain, on the location of the plant. For instance, if we take a concentrating plant, it must have adequate water supply, it must have space where tailings can be floated out from the plant. As to how closely we can place that to the mine, you can be sure that we will place it just as close to the mine as we can.

Senator KERR. Within 10 miles, 5 miles, 100 miles, or 1,000 miles?

Mr. FERNALD. Well, 10 miles, 20 miles, perhaps in very rare cases it might run up to 30 miles.

Senator KERR. Up to 30 miles?

Mr. FERNALD. Yes. There is no intention to have this run to a thousand miles. I do not think you will ever find a case where a thousand miles was the nearest place.

Senator KERR. It would not apply then to minerals obtained from some other country and shipped to a mill in the country?

Mr. FERNALD. No. *I think that would not be normal processing. It is what the normal operators do under those conditions as a normal treatment process.* But this proposed amendment would say if you move it off the edge of the property, *bing*, that is out. [Italics supplied.]

Senator KERR. I want to say that your position is well taken, if I understand it, and I wanted to be sure that I did understand it.

[781]

Senator MILLIKIN. *Mr. Fernald, you were going to give us illustrations of the processing which occurs after you get the ore out of the ground, which is involved in this question of transportation. Would you mind doing that? Give us a couple of illustrations.* [Italics supplied.]

Mr. FERNALD. We have the mining property here. Perhaps it may be at the top of a hill. There is no place there to locate a mill for handling that product. It is brought down the hill.

Senator MILLIKIN. *What I am trying to develop is, what is actually done with the ore to process it? I*

think you have made that part [782] of it very clear, but what are these processing things so that the members of the committee may understand it? [Italics supplied.]

Mr. FERNALD. I see.

For instance, for our ordinary metal mines there is the concentrating of the ore by gravity or by flotation. That is, the ore as it comes out of the ground is too low grade to be profitably shipped any distance. [Italics supplied.]

Senator MILLIKIN. There is a lot of dead rock in it?

Mr. FERNALD. It has rock in it. Of course, with some mines they will have an actual selection underground so that a lot of the waste will be left in the mine whereas the vein itself and the good ore will be hoisted to the surface. In other places, instead of trying to do any sorting underground the whole thing is sent to the mill and there, either by flotation or other concentrating processes, mechanically you eliminate a large amount of the waste rock and get the concentrates which carry the bulk of the mineral which can then be profitably shipped. [Italics supplied.]

Senator MILLIKIN. You are preparing your ores so that you have something to sell; that is the point, is it not? [Italics supplied.]

Mr. FERNALD. That is it exactly. [Italics supplied.]

Senator MILLIKIN. If you do not prepare them, you have nothing to sell and you do not have any income? [Italics supplied.]

Mr. FERNALD. That is the ordinary mining process. [Italics supplied.]

Senator MILLIKIN. Do you intend to carry it on to the smelting point? [Italics supplied.]

**Mr. FERNALD.** *When the amendment was originally presented in 1932 that matter was considered at some length and the Treasury felt strongly it should not include smelting as an ordinary treatment process applicable to percentage depletion. So the smelting of that ore was not originally treated as includible in the percentage depletion in gross income from mining. [Italics supplied.]*

**Senator MILLIKIN.** Smelting is another step?

**Mr. FERNALD.** *Smelting is another step. Even if you have a smelter right at the mine, that still has been held by the Treasury in a ruling which has stood ever since 1932 as not one of the ordinary treatment processes to be considered as mining. [Italics supplied.]*

**Senator MILLIKIN.** *So that all you are asking for is that transportation be included to that point where you can render your ore marketable? [Italics supplied.]*

**Mr. FERNALD.** *That is it. [Italics supplied.]*

**Senator MILLIKIN.** *That is the point? [Italics supplied.]*

**Mr. FERNALD.** Yes.

For coal, as they spoke this morning, they have this proposition of washing and classifying as part of their process. [Italics supplied.]

[783] Statement of SAM H. WILLISTON, Los Altos, Calif., chairman of the tax committee, Mining and Metallurgical Society of America:

[785]

**Senator CONNALLY.** What do you mean by shipping mines?



Mr. WILLISTON. Those are mines producing ore and shipping to a smelter.

S. Rep. No. 2375

(81st Cong., 2d Sess. (1950-2 Cum. Bull. 483))

[52]

## XI. OTHER ADJUSTMENTS IN THE TAX LAW

### (A) MEASURES CONTAINED IN THE HOUSE BILL

#### (1) *Percentage Depletion*

Section 204 of the House bill would amend section 114(b) of the code dealing with percentage depletion. The percentage allowed coal would be increased from 5 to 10; a number of items would be added to the list of nonmetallic minerals receiving the 15-percent rate; and a new group of nonmetallic minerals would receive percentage depletion at the rate of 5 percent. The House bill also includes an amendment intended to redefine the gross income upon which the percentage depletion rate is applied.

Section 208 of your committee's bill eliminates the increase in the rate on coal and the allowance of percentage depletion for the additional nonmetallic minerals enumerated in the House bill. An estimated revenue loss of \$35,000,000 annually is involved, which is difficult to reconcile with the need for revenue at the present time. Moreover, your committee is not convinced that all of the items to which percentage depletion would be extended have a valid claim to such treatment. In those cases where a valid claim for some additional depletion allowance exists, it is not evident that the percentage rates used in the House bill are necessarily the appropriate ones. Thus, it appears desirable to postpone action on these pro-

posals until your committee can carry out a more careful analysis of the problems involved.

Under the House bill the "gross income from the property" upon which percentage depletion is applied does not include any amount which reflects transportation beyond "the property." While this rule may be equitable when the *first processing* occurs on the property, it discriminates against the case where the *first processing* must be done elsewhere. Accordingly your committee has amended this provision so as to make it conform with what your committee believes is the intent of existing law. *The code section here involved was added in the 1943 Revenue Act so that the law would clearly have the same meaning as that intended by the depletion provisions in the 1932 act and contemporary Treasury regulations interpretative thereof.* Those regulations specified that the gross income computation for depletion [53] purposes was to be "before transportation from the place where the last of the processes listed below was applied." Terrain, water supply, or other factors, sometimes permit the application of ordinary treatment processes directly on the mining property. At other times the plants to apply such processes to obtain the commercially marketable mineral products are normally located some distance from the mouth or opening of the mine, but are at the nearest practicable point at which such processes can be efficiently performed. The transportation to these plants and the ordinary treatment processes applied are included as a part of mining in determining gross income for percentage depletion purposes. [Italics supplied.]

This rule, intended to be applied in accordance with normal standards, clearly would not extend to transportation to distant points far beyond the locations where mine operators would normally locate

such plants. But the rule would be applicable when the location of the plant or mill is at a point not substantially more distant from the point of extraction than is reasonably necessary for efficient and economical operation.

In order to remedy another problem pointed out to your committee at its hearings, the bill defines "ordinary treatment processes" in the case of bentonite to include crushing, drying, pulverizing or granulating, and loading for shipment.

The amendments made by this section of your committee's bill will be applicable to taxable years beginning after December 31, 1949.

H. Conference Rep. No. 3124

(81st Cong., 2d Sess. (1950-2 Cum. Bull. 580))

[7]

Amendment numbered 65:

That the House recede from its disagreement to the amendment of the Senate numbered 65, and agree to the same with an amendment, as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

**Sec. 207. PERCENTAGE DEPLETION.**

(a) *Transportation From Mine.*—The second sentence of section 114(b)(4)(B) (relating to the definition of gross income from property) is hereby amended to read as follows: "The term 'mining' as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores

or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills."

[8] (b) *Effective Date.*—The amendment made by subsection (a) shall be applicable with respect to taxable years beginning after December 31, 1959.

As the Senate agree to the same.

[21] STATEMENT OF THE MANAGERS ON THE  
PART OF THE HOUSE:

[26]

Amendment No. 65: The House bill (1) increased the percentage depletion allowance for coal, (2) allowed percentage depletion for the first time for certain minerals, and (3) provided that the gross income from mining upon which percentage depletion allowances are based should in no case include transportation beyond the property. The Senate amendment (1) strikes out these provisions of the House bill, (2) provides, effective with respect to taxable years beginning after December 31, 1949, that gross income from mining shall include transportation from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto, and (3) amends, effective with respect to taxable years beginning after December 31, 1946, the definition of "ordinary treatment processes" with respect to bentonite.

The House recedes with an amendment which eliminates those provisions of the Senate amendment relating to bentonite and limits the transportation permitted by the Senate amendment to be included as gross income from mining to so much of such transportation as does not exceed 50 miles unless the Secretary finds conditions to be such that the mineral must be transported to a greater distance to the plant or mill in which the ordinary treatment processes are applied.

\* \* \* \* \*

House Debate, 1950

(96 Cong. Record (Part 11))

81st Cong., 2d Sess.

[15590] Mr. JENKINS. \* \* \*

\* \* \* \* \*

Let us go a little further. Many of you were tremendously interested in depletion, allowances on gas, oil, clay, coal, and many other minerals that come from the earth. For years there has been a depletion allowance granted on these minerals. In the tax bill passed by the House we increased these depletion allowances and added a number of minerals to the list, including chemical limestone and a number of clays. It was thought proper at that time to do so. Now, the Senate in its desire to raise revenues cannot raise revenue by reducing revenue. So practically all of [15591] those depletion allowances the House made have been lost. They have been lost so that those who would have received them may count these losses as a contribution to meet the expenses of the war in Korea.

\* \* \* \* \*

Mr. CASE of South Dakota. I have read the conference report, particularly the depletion section, and



I want to commend the gentleman from Ohio and those who assisted for working out the provision which permits up to 50 miles transportation in computing depletion allowances where that transportation is necessary to get the materials to the processing plant. In processing clays, it is impossible to have a plant set on every quarter section where the material is located. The gentleman will recall that when the tax bill was up for consideration in the House the latter part of June he and I had a colloquy on this matter. The gentleman expressed his interest in the matter and suggested it could be worked out in conference. I appreciate what the gentleman from Ohio and others have done to work out a satisfactory provision.

Mr. JENKINS. I thank the gentleman for his contribution. To explain what it means a little more definitely to those of you who live in clay-producing and coal-producing sections and oil-producing sections where depletion allowances are permitted. If a brick plant, for instance, has to get its clay say 2 or 3 miles from the factory where it is processed the cost of manufacturing the brick should include the cost of transporting that clay. If you are not allowed a depletion allowance for the cost of transporting the principal material used in your manufacturing process then your depletion allowance does not cover the real cost of production. However, in the preparation of the new bill language has been inserted that provides a depletion allowance for transportation. The distance is limited to 50 miles, and there are some other conditions that must be met that I cannot now explain. This transportation allowance will apply more particularly in the western part of the country where they are required

to haul materials a longer distance to the place where processing is effected.

Mr. REED of New York. Many of these products upon which depletion is being asked have no value until they reach the processing plant; is that correct?

Mr. JENKINS. Yes; without the depletion allowance we would not have much of the materials and minerals that are now processed into valuable articles of commerce.

\* \* \* \* \*

Revenue Act of 1950

(c. 994, 64 Stat. 906, 931 (approved September 23, 1950))

SEC. 207. PERCENTAGE DEPLETION.

(a) *Transportation From Mine.*—The second sentence of section 114(b)(4)(B) (relating to the definition of gross income from property) is hereby amended to read as follows: "The term 'mining' as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills."

(b) *Effective Date.*—The amendment made by subsection (a) shall be applicable with respect to taxable years beginning after December 31, 1949.

1951

[After hearings which were largely a repetition of those held the prior year, percentage depletion was allowed for various additional minerals. Again, to a large extent, the testimony at the hearings related to the mining, processes applied, and uses of the minerals. The pertinent portions thereof are omitted here but included in Part B of this Appendix. Other portions of the hearings and debates, as well as the legislative reports and the statute as enacted, are set forth below in sequence.]

House Hearings, 1951

(Revenue Revision of 1951, Hearings Before the Committee on Ways and Means, House of Representatives, 82d Cong., 1st Sess. (Part 3))

[1537] Statements of J. Rutledge Hill, Dallas, Tex., Chairman of the Committee on Taxation, National Sand and Gravel Association, and Charles E. Brady, Salisbury, N.C., Vice Chairman of the Committee on Taxation, National Sand and Gravel Association:

Mr. HILL. In behalf of the commercial sand and gravel industry of the United States, I ask your committee to recommend to the House that sand and gravel be added to the list of nonmetallic minerals entitled to percentage depletion.

[1539] Our industry believes that percentage depletion for the mining industry is sound public policy. We also believe that sand and gravel should be brought under that policy, for the reasons which I have stated. It seems to us an unreasonable discrimination against our industry to continue to be denied

the benefit of a taxation policy already extended to other members of the nonmetallic minerals family.

[1540] Mr. BRADY. Chairman Doughton and members of the Ways and Means Committee, I am Charles E. Brady, sales manager for four gravel and sand plants in North Carolina.

Mr. Hill, who preceded me, has covered the essential points which stress our urgent need for an adequate percentage depletion allowance. In North Carolina we have experienced a greatly accelerated depletion of our known gravel and sand deposits within the last year and a half.

[1541] Mr. JENKINS. There are no really large sand and gravel companies, are there, such as you run into in the big steel companies?

Mr. HILL. That is correct. They are usually very small operators as you would describe a business enterprise.

[1542] Statement of JAMES W. HALEY, Secretary, Special Tax Committee, National Coal Association, Washington, D.C.:

[1544] We are here today to urge the Congress to reduce this inequitable treatment between coal and its competitors by increasing the depletion rate for coal to 10 percent.

[1553] Statement of RALPH L. DICKEY, President, The Kelley Island Lime & Transport Co., Cleveland, Ohio:



[1553-1554] I am a representative of a committee of the National Lime Association and am requesting that a percentage depletion allowance be provided for metallurgical and chemical grade limestone at a rate of 15 percent. \* \* \*

[1571] Statement of Donald A. Callahan, Representing the American Mining Congress, Washington, D.C.:

I am addressing myself particularly to the subject of percentage depletion and the rates for metal mines as set forth in the amendment to the revenue laws adopted in 1932. I also wish to address myself to the subject of depletion generally as applied to mines.

As the committee is well aware, the 1932 amendment provides for depletion allowance in the following language:

The allowance for depletion shall be in the case of metal mines 15 percent \* \* \* of the gross income from the property during the taxable year.

Perhaps it would be well at the outset to review briefly the experience which formed the basis for the 1932 amendment. Depletion allowances in natural resource industries have been recognized since the adoption of the income-tax amendment in 1913. Such allowances were based upon the fact that earnings from such industries could only be obtained through the using up of the resources themselves and that such consumption resulted ultimately in the complete exhaustion of the resources which constituted the assets of the taxpayer. It had been early recognized that depletion should not be based solely on cost or March



1, 1913, value, but that the value of discovered minerals should in itself be a basis for allowable depletion. It was correct in theory to give this recognition to the exhaustion of the capital asset. It was essential in practice that this should be done if we were to have a continuing and expanding mineral industry and to deal fairly with it. The difficulty was as to the technicalities introduced and the methods employed.

Prior to 1926 when the principle of percentage depletion was first applied to the oil and gas industry, and to 1932 when it was first applied to metal mining, the method employed in determining a proper allowance for depletion was this: First, an estimate was arrived at of the number of recoverable units in the property. Then through a very involved analytic process the present worth of each unit as of the date of valuation was calculated, and this multiplied by the number of units extracted each year was the basis for the depletion allowance. This process involved the use of many unknown and unknow-[1572] able factors, and resulted in great uncertainties and inequalities. It was an involved, difficult, and costly method of determining depletion allowance.

The oil and gas industry was granted a depletion allowance based upon a percentage of its gross income in the Revenue Act of 1926. At the same time metal miners sought to secure similar treatment. The Congress decided that it had not sufficient evidence upon which to establish an equitable rate and later the staff of the Joint Committee on Internal Revenue Taxation prepared an exhaustive report. *This report, popularly known as the Parker Report, is the basis upon which the rate of 15 percent for metal mines was finally established in the Revenue Act of 1932.* The report showed that the average allowance for a con-

siderable period of time in the case of metal mines had been approximately 17 percent under the old methods employed. The metal mining industry accepted a rate of 15 percent as equitable at that time and this rate has prevailed since. [*Italics supplied.*]

The old methods in use before percentage depletion was written into the law involved complicated processes for determining the present value of the units contained in the ground. I do not need to tell you how difficult and untrustworthy such processes were. I do not need to tell you what engineering and scientific staffs were required by the Bureau of Internal Revenue to check returns which were furnished by [1573] engineering, scientific and accounting staffs which the mining companies found it necessary to employ in order to make a satisfactory return. It was largely because of these difficulties that the *simple method* of determining the amount of depletion each year through a percentage based upon the *gross values of the ore produced* was agreed upon. *Through this method the small producer is on a par with the larger operator who could provide the necessary technical staff.* The Bureau of Internal Revenue was provided with a simple method of determining the amount to be allowed. *Discriminations as between individual producers of the same metal were eliminated.* Percentage depletion has added materially to the revenue derived by the Government and has decreased the cost of its collection. [*Italics supplied.*]

What we of the mining industry ask is that there be no curtailment of the *modest* depletion allowance now effective, but rather an increase in such allow-

ance and a liberalization of the laws applicable to mining operations \* \* \*. [Italics supplied.]

[1574] I also ask, gentlemen, to be permitted to file a booklet on Mining Taxation, prepared by the American Mining Congress in February 1950, and a statement on "Depletion of Mines," recently prepared by the same organization.

The CHAIRMAN. Without objection, that will be done. We thank you for your appearance and the information you have given the committee.

(The documents referred to are as follows:)

**MINING TAXATION—CHANGES IN FEDERAL TAX LAWS  
NEEDED TO ENCOURAGE MINING ENTERPRISE**

**[1577] IV. ADEQUATE ALLOWANCES FOR PERCENTAGE  
DEPLETION**

The percentages used in computing percentage depletion, both with respect to gross income and with respect to net income, should be increased.

Percentage depletion was first granted to mines in 1932 as *a simple and equitable means of measuring the exhaustion of the capital value of the mineral deposit* during the life of the mine—without the technicalities of the unit-depletion method based on cost, discovery value, etc. The allowance for depletion in the case of metal and some nonmetallic mines is computed at 15 percent of the gross income from the property, but not more than 50 percent of the net income from the property. The 15 percent rate was somewhat less than the average depletion which had previously been allowed for metal mines, as deter-

mined by careful studies by Government engineers.  
[Italics supplied.]

[1579]

#### DEPLETION OF MINES

(A statement by the mining industry.)

[1581] 3. *The depletion allowance is merely a means for returning to the owner or producer of minerals the capital consumed in the enterprise.*

4. *Percentage depletion resulted from a careful study by Congress. It affords the simplest and best method for determining the annual consumption of capital in the mineral-extractive industries.*

After years of difficult experience with other methods of computing depletion allowances for mines, Congress in 1932 adopted the percentage method for metal mines, coal and sulfur deposits. Previously, in 1926, the percentage basis for depletion had been adopted for oil and gas, and reports by the staff of the Joint Committee on Internal Revenue Taxation and by the Treasury Department showed that it had "functioned satisfactorily both from the economical and administrative viewpoints and without loss to the Government."

The joint committee held extensive hearings, and its technical staff made extensive studies on the subject of mine-depletion allowances. Printed reports of the hearings and of the staff studies and recommendations were fully considered by Congress in adopting the percentage method and the rates. \* \* \*

[1582]

## CONCLUSION

Percentage depletion, *by its simplicity and obvious fairness*, permits substantial savings in administration to both Government and taxpayer; it *avoids discrimination* against smaller taxpayers; it is a protection against the excessive taxation of capital; it is *the simplest and best procedure* yet devised for sustaining capital investment in an industry that is vital to our national welfare and security. [Italics supplied.]

[1583] Statement of WESLEY E. DISNEY, Representing Eastern Magnesia Talc Co., Burlington, Vt.

(Mr. Disney later filed the following statement:)

Statement of WESLEY E. DISNEY in support of percentage depletion allowance for talc producers.

There is a striking similarity in the problems of finding, developing, producing, and processing of talc and that of metallic minerals with the additional difficulty that talc quite often occurs in nature in much smaller deposits than the metallics. All the elements of risk involved in metal mining are present in talc mining, but this is coupled with the fact that the talc industry is composed of small business and because of the variety of grades and types of talc, each producer must process to the exacting customer requirements and must sell directly to the consumer.



(82d Cong., 1st Sess. (1951) (1951-2 Cum. Bull. 357))  
[29]

### I. PERCENTAGE DEPLETION

Under existing law depletion based on cost is available to all mining industries and in addition percentage depletion is available to oil, gas, sulfur, metal mines, and certain nonmetallic minerals. The allowable rate of percentage depletion is 5 percent in the case of coal, and 15 percent in the case of the other nonmetallic minerals except sulfur which is allowed 23 percent.

The testimony received by this committee both in connection with this bill and the bill which became the Revenue Act of 1950 revealed that in a number of cases nonmetallic minerals which are not in the enumerated group under existing law are competitive with those receiving percentage depletion, or have just as good a claim for such [30] treatment as the enumerated minerals. The testimony also indicated that the 5-percent rate allowed coal is of little practical value, and that the coal mining industry is peculiarly in need of more favorable tax treatment because of the inroads which alternative sources of energy, particularly oil and gas, have made on the potential markets of coal. [Italics supplied.]

Section 304 of this bill adds to the list of nonmetallic minerals to which percentage depletion is available at a 15-percent rate, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, perlite, diatomaceous earth, and metallurgical and chemical grade limestones. The amendment also makes it clear that the 15-percent rate applies to thenardite, whether or not obtained from brines, or mixtures of brine.

The bill increases the percentage allowed in the case of coal from 5 to 10 percent, and sets up a new group

of minerals to which percentage depletion is available at the rate of 5 percent. This group consists of sand, gravel, stone, including pumice, scoria, and slate, brick and tile clay, shale, oyster shell, clam shell, granite, marble and asbestos.

*Most of these changes would have been made under the House version of the bill which became the Revenue Act of 1950 but they were eliminated from the final legislation largely because of the revenue loss involved. It is apparent, however, that the need for equalization is substantially greater now because of the additional taxes imposed under the legislation of 1950 and under this bill. Therefore, the committee believes that the proposed extension of the percentage depletion system is necessary in spite of the revenue loss involved. The latter is estimated to be about \$67 million in a full year's operation. [Italics supplied.]*

The amendments made by this section of the bill apply to taxable years beginning after December 31, 1950.

\* \* \* \* \*

[67]—DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL

\* \* \* \* \*

[114] SEC. 304. PERCENTAGE DEPLETION.

This section of the bill grants a percentage-depletion allowance at the rate of 5 percent in the case of deposits of asbestos, sand, gravel, granite, marble, stone (including pumice, scoria, and slate), brick clay, tile clay, shale, clamshell, and oystershell. Percentage-depletion allowance is also provided in the case of deposits of tripoli, borax, fuller's earth, refractory and fire clay, quartzite, perlite, diatomaceous earth, metallurgical-grade limestone, and chemical-grade limestone, at the rate of 15 percent. The 5-percent

rate of percentage depletion now allowed for coal has been increased to 10 percent. The allowances are of the stated percentages of the gross income from the property but not in excess of 50 percent of the net income (computed without allowance for depletion) from the property.

Subsection (b) of this section makes a technical amendment to paragraph (2) of section 114(b) of the code in order to eliminate the necessity of listing by name those mines for which depletion based on discovery value is denied by reason of the allowance of percentage depletion.

Your committee has made technical amendments to section 114(b) (4) (A) which do not alter its substance. A change has also been made in the parenthetical clause stating the source from which thenardite is derived. Under the present wording of the section, percentage depletion is allowed for thenardite produced from brines or mixtures of brine. To remove any ambiguity your committee has changed the wording of this section so that thenardite, including thenardite from brines or mixtures of brine, is permitted the percentage depletion allowance.

The amendments made by this section of the bill shall apply only with respect to taxable years beginning after December 31, 1950.

House Debate, 1951

(97 Cong. Record (Part 5), 82d Cong., 1st Sess.)  
[6889]

REVENUE ACT OF 1951

Mr. DOUGHTON. \* \* \*

[6890] This is the setting, then, in which we ask favorable consideration of the pending bill, which includes the following major provisions:

[6891]

Fourth. Percentage depletion: Another relief provision is one granting percentage depletion to certain new minerals, and increasing percentage depletion in the case of coal from 5 percent to 10 percent. The following new group of minerals is allowed percentage depletion at the rate of 5 percent: Sand, gravel, stone—including pumice, scoria, slate—brick and tile clay, shale, oyster shell, clam shell, granite, marble, and asbestos.

The following minerals are added to the list of minerals receiving a 15-percent depletion allowance: Borax, fuller's earth, tripoli, refractory and fire clay, quartzite, perlite, diatomaceous earth, and metallurgical and chemical grade limestone.

Many of these minerals compete with minerals now being granted a depletion allowance, and *the committee thought it desirable to place such minerals on a competitive basis as far as the depletion allowance is concerned.* [Italics supplied.]

S. Rep. No. 781

(82d Cong., 1st Sess. (1951) (to accompany H.R. 4473) (1951-2 Cum. Bull. 458))

[37] 6. *Percentage depletion.*

Under existing law depletion based on cost is available to all mining industries and in addition percentage depletion is available to oil, gas, sulfur, metal mines, and certain nonmetallic minerals. The allowable rate of percentage depletion is 5 percent in the case of coal, and 15 percent in the case of the other

nonmetallic minerals except sulfur which is allowed 23 percent.

The testimony received by this committee both in connection with this bill and the bill which became the Revenue Act of 1950 revealed that in a number of cases nonmetallic minerals which are not in the enumerated group under existing law *are competitive with those receiving percentage depletion, or have just as good a claim for such treatment as the enumerated minerals.* The testimony also indicated that the 5-percent rate allowed coal is of little practical value, and that the coal mining industry is peculiarly in need of more favorable tax treatment because of the inroads which alternative sources of energy, particularly oil and gas, have made on the potential markets of coal. [Italics supplied.]

Both section 319 of your committee's bill and section 304 of the House bill set up a new group of minerals to which percentage depletion is available at the rate of 5 percent. Both bills extend this rate to sand, gravel, slate, stone (including pumice and scoria), brick and tile clay, shale, oyster shell, clam shell, granite, and marble. In addition, your committee has added to this category entitled to the 5-percent rate sodium chloride, and, if from brine wells, calcium chloride, magnesium chloride, potassium chloride, and bromine. In the allowance of percentage depletion for these items, your committee does not intend to reduce allowances now granted. For example, potash is allowed percentage depletion at 15 percent under present law, and your committee does not intend to reduce this allowance with respect to potash or any of its salt derivatives which are presently receiving percentage depletion at 15 percent. The bill also makes a technical change in this portion of the House provision by including slate as a separate item rather



than including it as a type of stone as in the House bill.

The House bill also included asbestos at the new 5-percent rate. Because of the importance of this product and the smallness of its supply in this country, your committee has allowed asbestos a 10-percent rate. Both bills increase coal from its present 5-percent rate to 10 percent.

[38] The House bill added to the list of nonmetallic minerals, to which percentage depletion is available at a 15-percent rate, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, perlite, diatomaceous earth, and metallurgical and chemical grade limestones. Your committee's bill, on the other hand, provides that these items added by the House are to receive percentage depletion at the same 10-percent rate accorded coal and asbestos. In addition to these items, your committee has added a 10-percent rate for wollastonite, which is important as an insulating and fireproofing material and *thus competitive* with other items presently accorded similar treatment, and the magnesium compounds magnesite, dolomite, and brucite. [Italics supplied.]

Your committee's bill adds to the nonmetallic minerals presently receiving 15-percent depletion, aplite. This material, which is found in only small quantities in this country, is closely related to feldspar, which already receives 15-percent depletion.

Your committee has also made two technical revisions in the 15-percent depletion section of the House bill. The latter includes at the 15-percent rate "thenardite (including thenardite from brines or mixtures of brine.)" Your committee has eliminated the parenthetical limitation as unnecessary and because it might give rise to doubt as to certain other of the enumerated products. For example potash, trona,

and borax are also frequently recovered from brines or mixtures of brine. The phrase "mines and other natural deposits" is clearly broad enough to include brines as well as all other natural sources. The particular type of source is immaterial.

The names of all the various enumerated minerals are of course intended to have their commonly understood commercial meaning. For example, the term "thenardite" applies to sodium sulphate, also known as salt cake; the term "trona" to sodium carbonate and sodium bicarbonate, also known as soda ash; and the term "borax" to boron minerals generally.

Your committee has also amended the House provision which reads "ball and sagger clay" to read "ball clay, sagger clay" in order to remove the implication of the House bill that these are not separate types of clay.

*Many of the above changes were provided in the House version of the bill which became the Revenue Act of 1950 but they were eliminated by your committee and from the final legislation largely because of the revenue loss involved. It is apparent, however, that the need for equalization is substantially greater now because of the additional taxes imposed under the legislation of 1950 and under this bill. Therefore, the committee believes that the proposed extension of the percentage depletion system is necessary in spite of the revenue loss involved. The latter is estimated to be about \$76 million in a full year's operation. [Italics supplied.]*

The amendments made by this section of the bill apply to taxable years beginning after December 31, 1950.

(82d Cong., 1st Sess. (1951) (1951-2 Cum. Bull. 545))

[1] DETAILED DISCUSSION OF THE TECHNICAL PROVISIONS OF THE BILL

[37] SEC. 319. PERCENTAGE DEPLETION.

This section corresponds to section 304 of the bill as passed by the House. The House bill granted a percentage depletion allowance at the rate of 5 percent in the case of deposits of asbestos, sand, gravel, stone (including pumice, scoria, and slate), brick clay, tile clay, shale, oyster shell, clam shell, granite, and marble. Your committee has granted percentage depletion in the case of asbestos at the rate of 10 percent and has added to the above list sodium chloride and, if produced from brine wells, calcium chloride, magnesium chloride, potassium chloride, and bromine. Your committee has removed slate from the parenthetical clause following stone and has included it as a separate item in this 5-percent category. The House bill increased the 5-percent rate of percentage depletion now allowed for coal to 10 percent. Your committee has followed this treatment in the case of coal and has included in this new 10-percent category those minerals which the House bill would have allowed percentage depletion at a rate of 15 percent. These minerals are borax, fuller's earth, tripoli, refractory and fire clay, quartzite, perlite, diatomaceous earth, metallurgical grade limestone, and chemical grade limestone. Your committee has also added wollastonite, magnesite, dolomite, and brucite to this 10-percent list, and has added aplite to the listed materials now allowed percentage depletion at the 15-percent rate.

Subsection (b) of this section makes a technical amendment to paragraph (2) of section 114(b) of the code in order to eliminate the necessity of listing by name those mines for which depletion based on discovery value is denied by reason of the allowance of percentage depletion.

Your committee has made technical amendments to section 114(b)(4)(A) which do not alter its substance. The House bill changed the parenthetical clause, stating that thenardite produced from brines or mixtures of brine would be allowed percentage depletion, to state that thenardite, including thenardite from brines or mixtures of brine, would be permitted such allowance. Your committee believes that the same effect can be achieved by striking the parenthetical clause.

The amendments made by this section shall be applicable only with respect to taxable years beginning after December 31, 1950.

H. Conference Rep. No. 1213

(82d Cong., 1st Sess. (1951)(1951-2 Cum. Bull. 622))

[17] Amendment numbered 53: That the House recede from its disagreement to the amendment of the Senate numbered 53, and agree to the same with an amendment as follows:

In lieu of the matter proposed to be inserted by the Senate amendment insert the following:

“(i) in the case of sand, gravel, slate, stone (including pumice and scoria), brick and tile clay, shale, oyster shell, clam shell, granite, marble, sodium chloride, and, if from brine wells, calcium chloride, magnesium chloride, and bromine, 5 per centum,

“(ii) in the case of coal, asbestos, brucite, dolomite, magnesite, perlite, wollastonite, cal-

*cium carbonates, and magnesium carbonates, 10 per centum,*

*"(iii) in the case of metal mines, aplite, bauxite, fluorspar, flake graphite, vermiculite, beryl, garnet, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, ball clay, sagger clay, china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite, thenardite, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, diatomaceous earth, metallurgical grade limestone, chemical grade limestone, and potash, 15 per centum, and*

And the Senate agree to the same.

[76] Amendment No. 53: The House bill granted a percentage depletion allowance at the rate of 5 percent in the case of deposits of asbestos, sand, gravel, stone (including pumice, scoria, and slate), brick clay, tile clay, shale, oyster shell, clam shell, granite, and marble. The Senate amendment granted percentage depletion in the case of asbestos at the rate of 10 percent and added to the above list sodium chloride and, if produced from brine wells, calcium chloride, magnesium chloride, potassium chloride, and bromine. The Senate amendment removed slate from the parenthetical clause following stone and included it as a separate item in this 5-percent category. The House bill increased the 5-percent rate of percentage depletion now allowed for coal to 10 percent. The Senate amendment followed this treatment in the case of coal and included in this new 10-percent category those minerals which the House bill would have allowed percentage depletion at a rate of 15 percent. These minerals are borax, fuller's earth, tripoli, refractory and fire clay, quartzite, perlite, diatomaceous earth, metallurgical grade limestone, and chemical



grade limestone. The Senate amendment also added wollastonite, magnesite, dolomite, brucite, and calcium and magnesium carbonates, to this 10-percent list, and added aplite and garnet to the list now allowed percentage depletion at the 15-percent rate.

The bill, as passed by both the House and the Senate, made technical amendments to section 114 (b)(4)(A) which do not alter its substance. The House bill changed the parenthetical clause, stating that thenardite produced from brines or mixtures of brine would be allowed percentage depletion, to state that thenardite, including thenardite from brines or mixtures of brine, would be permitted such allowance. The Senate amendment achieved the same effect by striking the parenthetical clause.

The amendments made by both Houses are applicable only with respect to taxable years beginning after December 31, 1950.

The House recedes with an amendment which restores borax, fuller's earth, tripoli, refractory and fire clay, quartzite, diatomaceous earth, metallurgical grade limestone, and chemical grade limestone to the 15-percent category in which they appeared in the House bill and which removes potassium chloride from the list of minerals to which [77] the Senate bill granted the percentage depletion allowance at the 5-percent rate. Potassium chloride is entitled, under existing law, to percentage depletion allowance at 15 percent. Under the conference agreement calcium carbonates are granted an allowance of 10 percent, while marble, which is a calcium carbonate, receives 5 percent. It is intended, in any case where a mineral is specifically provided for at a stated rate of percentage allowance, that the specific provision will govern over the allowance provided (whether higher or lower) for a more general classification.

It is the intention, in including stone in the 5 percent percentage depletion category, to limit such term to its commonly understood meaning. Thus, depletion would be allowed in the case of common stone which is crushed for use in building roads but would not be allowed in the case of precious stones such as diamonds.

Revenue Act of 1951

(c. 521, 65 Stat. 452, 497 (approved October 20, 1951))

SEC. 319. PERCENTAGE DEPLETION.

(a) *Allowance of Percentage Depletion.*—So much of paragraph (4) of section 114(b) as precedes the last sentence of subparagraph (A) is hereby amended to read as follows:

“(4) *Percentage depletion for coal and metal mines and for certain other mines and natural mineral deposits.*—

(A) *In general.*—The allowance for depletion under section 23(m) in the case of the following mines and other natural deposits shall be—

“(i) in the case of sand, gravel, slate, stone (including pumice and scoria), brick and tile clay, shale, oyster shell, clam shell, granite, marble, sodium chloride, and, if from brine wells, calcium chloride, magnesium chloride, and bromine, 5 per centum,

“(ii) in the case of coal, asbestos, brucite, dolomite, magnesite, perlite, wollastonite, calcium carbonates, and magnesium carbonates, 10 per centum,

“(iii) in the case of metal mines, apatite, bauxite, fluor spar, flake graphite, vermiculite, beryl, garnet, feldspar, mica, talc (including phyllosilicates), lepidolite, spodumene, barite, ball clay, sagger clay, china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite,

thenardite, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, diatomaceous earth, metallurgical grade limestone, chemical grade limestone, and potash, 15 per centum, and

"(iv) in the case of sulfur, 23 per centum, of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the property."

(b) *Technical Amendment.*—So much of paragraph (2) of section 114(b) as precedes "discovered by the taxpayer after February 28, 1913" is hereby amended to read as follows:

"(2) *Discovery value in the case of mines.*—In the case of mines (except mines in respect of which percentage depletion is allowable under paragraph (4) of this subsection)".

(c) *Effective Date.*—The amendments made by this section shall be applicable only with respect to taxable years beginning after December 31, 1950.

#### 1953-1954

[In Section 613(c) of the Internal Revenue Code of 1954 the definition of "gross income from the property" was continued in its same form except for minor additions to the definition of "ordinary treatment processes." Adoption of the Code was preceded by hearings at which some statements were submitted on percentage depletion. The pertinent portions of the legislative reports and hearings are set forth below in sequence.]

## House Hearings, 1953

(General Revenue Revision, Hearings before the Committee on Ways and Means, House of Representatives, 83d Cong., 1st Sess. (Part 3))

[1982]

Statement of HENRY B. FERNALD, Montclair, N.J., Chairman, Tax Committee, American Mining Congress:

[1986]

### THREE-YEAR EXEMPTION FOR NEW MINES

The CHAIRMAN. I would like to ask you another question, Mr. Fernald.

Do you think, in defining minerals, we should be careful to separate the value added by manufacturing?

[1987]. Mr. FERNALD. I think as we speak of manufacturing, as you and I are dealing with the use of that term, I can say, "Yes; I think we should." However there are very many processings of these minerals which I would never think of as being manufacturing, and I do not think you would, and yet which many do argue should be excluded because it is a manufacturing process.

*The ordinary treatment processes which are normally applied to bring your minerals into a marketable condition I do not think should be talked of as manufacturing costs. [Italics supplied.]*

The CHAIRMAN. I agree with you on that; because, for instance, they have mines up in my State where

the product cannot be sold until it is ground fine enough to go into the market.

[2033]

Statement of HENRY MULRYAN, president, Sierra Tale & Clay Co., South Pasadena, Calif.:

[2035] Although no blending, concentration, or other beneficiation is required, with the exception of a single operation in Vermont, tale must be ground to be salable. \* \* \* Substantially all tale sales are made by the mine operator directly to the ultimate consumer. There is practically no commercial use for the raw ore until it has been finely ground. \* \* \*

[2036] The CHAIRMAN. Pardon me. Not only in the fact of the statute itself, but without grinding you could not sell the tale in your State?

Mr. MULRYAN. That is correct. Practically all of it has to be fine ground to be marketable.

[2037] We therefore ask that section 114(b)(4)(B)(iv) be amended to add "tale" to the list of minerals now contained in that subsection. We think this addition would make clear that Congress intended in section 114 that in the case of tale which is not customarily sold in its crude form, the term "ordinary treatment processes" includes crushing and all grinding *necessary to bring the product to a commercially marketable state. We think that is precisely what the law says today and what Congress intended, because when the law was amended in 1947 to include tale on a permanent basis, Congress acted in the light of testimony by the industry which showed clearly*



that tale is not customarily sold in its crude form, and that it must undergo fine grinding to get it into a marketable state. [Italics supplied.]

[2070] Statement of RUSSELL P. HEUER, representing the Refractories Institute:

Mr. HEUR. My name is Russell P. Heuer. I am vice president of General Refractories Co., Philadelphia, Pa. I represent the Refractories Institute, a national association of 87 refractory manufacturers, and this statement is made in behalf of its members and the entire refractories industry. I wish to cite the benefits to the national economy which have been derived from the granting of the allowance for percentage depletion to refractory and fire clays and quartzite by the 1951 Revenue Act and to urge the retention of this provision in its present form.

The specific Internal Revenue Code provision to which I refer is section 114(b)4(A), which was amended by Congress in Public Law 183, 82d Congress, 1st session, by the addition of "refractory and fire clays, quartzite" to the minerals subject to percentage depletion.

#### MINERALS USED IN THE MANUFACTURE OF REFRACTORIES

Refractory products are *manufactured* from carefully selected minerals, the chief minerals being refractory and fire clay and quartzite. The raw minerals are crushed, ground, and blended, and then made into brick and shapes for use in furnace construction. [Italics supplied.]

[2072] ADMINISTRATION OF THE ALLOWANCE OF PERCENTAGE DEPLETION OF REFRACTORY MINERALS

The refractory industry has generally adopted the view that "ordinary treatment processes" as that term is used in the Internal Revenue Code, section 114(b)4(B), includes in the term "mining," in the case of refractory and fire clays and quartzite, the process of crushing, grinding, screening, and blending of the raw minerals.

Regulations 111, section 29.23(m)-1(f) as amended by the Treasury Department on July 14, 1953 are not inconsistent with the view of the industry.

The industry further believes that the attitude of its members as to the technical provisions relating to the computation of percentage depletion has been fair and reasonable. The industry, therefore, respectfully submits that the present percentage depletion provisions relating to refractory and fire clays and quartzite should be retained in their present form and urges your committee to adopt this conclusion in its consideration of possible amendments to the Internal Revenue Code.

H. Rep. No. 1337

(83d Cong., 2d Sess. (1954) (on Internal Revenue Code of 1954, H.R. 8300) (3 U.S.C. Cong. & Adm. News (1954) (4017, 4084))

[58] B. *Definition of income from property* (sec. 613(c))

Under present law and the bill, the gross income rates referred to above are applied to "gross income from the property." This is defined as gross income from mining, and "mining" in turn is defined as the

extraction of the minerals, the "ordinary treatment processes" normally applied to obtain commercially marketable mineral products and certain transportation. Present law also lists a number of specific processes that are considered to be ordinary treatment processes.

The bill continues these definitions except in three respects. In the case of magnesite, burning is to be regarded as an ordinary "treatment process" and in the case of talc, fine pulverizing is to be regarded as such a process. The present definition of "sulfur processing" is specifically related to the Frasch process, so that the general rule for ordinary treatment processes is to be available for sulfur produced in other ways.

\* \* \* \* \*

[A183] *Section 613. Percentage depletion.*

\* \* \* \* \*

[A185] Subsection (c) corresponds to section 114 (b)(4)(B) of the 1939 Code. Under existing law, the percentage rate of depletion is applied to "gross income from the property" and that term is defined in present law to mean in the case of a property other than an oil or gas well, the gross income from "mining." The term "mining" is defined in present law to mean not merely the extraction of the ores or minerals from the ground but also certain "ordinary treatment processes" applied by mine owners or operators and certain specified transportation. Existing law provides for separate categories of specific processes which are considered to be included within the term "ordinary treatment processes." The processes specified in the case of sulfur have been amended to indicate that the specified processes apply only to the recovery of sulfur by the Frasch process. In certain cases, sulfur may be recovered by

processes other than those specified in existing law which, in appropriate cases, may also be treated as "ordinary treatment processes."

In addition, this subsection amends existing law to specifically provide that the term "ordinary treatment processes" includes the pulverization of talc and the burning of magnesite.

\* \* \* \* \*

S. Rep. No. 1622

(83d Cong., 2d Sess. (1954) (On Internal Revenue Code of 1954, H.R. 8300) (3 U.S.C. Cong. & Adm. News (1954) 4621, 4711))

[79] B. *Definition of Income from Property (sec. 613(c)).*

(1) *House changes accepted by committee.*

\* \* \* \* \*

(2) *Changes made by committee.*

The term "ordinary treatment processes" in the case of coal was extended by the Committee to include "dust allaying and treating to prevent freezing." The latter process is now allowed under regulations. Also in the case of phosphate rock, "sintering and nodulizing" are included as an ordinary treatment process.

C. *Mine Tailings (sec. 613).*

(1) *House changes accepted by committee.*

Depletion allowances under present law are allowed with respect to mines and natural deposits. The House and your committee's bill extends percentage depletion at the appropriate rates to mine owners for minerals recovered from the residue that had accumulated from their mine. The provision does not apply in the case of a purchaser of such waste or residue or to a purchaser or rights thereto.

\* \* \* \* \*

[332] Section 613(c) of the bill as passed by the House corresponds to section 114(b)(4)(B) of the 1939 Code, under which the rate of percentage depletion is applied to "gross income from the property," and that term is defined to mean, in the case of a property other than an oil or gas well, the gross income from "mining." The term "mining" in existing law is defined to mean not merely the extraction of ores or minerals from the ground but also certain "ordinary treatment processes" applied by mine owners or operators and certain specified transportation. Existing law provides four separate categories of specific processes which are considered to be included within the term "ordinary treatment processes." The House bill amended existing law with respect to sulfur to indicate that the specified processes apply only to the recovery of sulfur by the Frasch process. In cases where sulfur is recovered by processes other than the Frasch process, such other processes will be allowed or disallowed as "ordinary treatment processes" in accordance with the general provisions of section 613(c). Your committee has amended section 613(c)(4)(A) to provide that in the case of coal dust allaying and treating to prevent freezing are considered ordinary treatment processes. The House bill amended existing law specifically to provide that the term "ordinary treatment processes" includes the pulverization of talc and the burning of magnesite. Your committee has added to this list "the sintering [333] and nodulizing of phosphate rock." In the case of uranium the gross income from the property for purposes of applying the percentage depletion allowance will be determined by reducing the sale price of the ore by the net transportation cost of the taxpayer. For this purpose, the net transportation cost means the taxpayer's transportation cost reduced by



the hauling allowance allowed by the Atomic Energy Commission.

**H. Conference Rep. No. 2543**

(83d Cong., 2d Sess. (1954) (on Internal Revenue Code of 1954, H.R. 8300) (3 U.S.C. Cong. & Adm. News (1954) 5280, 5313))

[52] Amendment No. 148: The House bill provided the following ordinary treatment processes in the case of coal: Cleaning, breaking, [53] sizing, and loading for shipment. The Senate amendment extends this list to include dust allaying and treating to prevent freezing. The House recedes.

Amendment No. 149: This amendment provides that sintering and nodulizing are ordinary treatment processes in the case of phosphate rock. The House recedes.

**Part II: Additional Legislative Materials: Excerpts from Hearings and Debates Indicating the Commercially Marketable Products to which the Proponents of Legislation had Reference in Seeking Percentage Depletion in relation to Particular Minerals.**

**ASBESTOS**

(Percentage depletion first allowed beginning with 1951)

**Senate Hearings, 1951**

(The Revenue Act of 1951, Hearings before the Committee on Finance, United States Senate, 82d Cong., 1st Sess., on H.R. 4473)

[866] Statement of M. V. ENGELBACK, Manager, Field Engineering, The Ruberoid Co.

— Asbestos is the only known mineral fiber, and the only known incombustible fiber. It occurs in several types, and its grades are based on fiber length. \* \* \*

[867] Asbestos is extremely scarce and hard to find in America. The only known deposits of commercial value are found in Georgia, Arizona, and Vermont. And just one mine in Vermont provides about 97 percent of our domestic production.

Asbestos mining is in the category of a "low grade" mining venture. In order to recover our Vermont production 1949 of only about 43,000 tons, we had to mine and process approximately 1,000,000 tons of ore, to say nothing of removal of waste. The average asbestos yield amounts to only 4 to 6 percent recovery.

Senator MILLIKIN. Is it a surface deposit, or do you mine it?

Mr. ENGELBACK. At present, it is a quarry operation, but shortly we shall have to go underground. In Arizona, it is an underground operation, but that accounts for practically nothing, sir.

Of that total the small amount of only 4 to 5 percent can be called long fiber, if we happen to find any at all.

[868] \* \* \* We cannot choose to mine either long fiber or short fiber. We have to take what comes. The only method of *separating* grades of fiber is by a highly specialized *milling* operation. [Italics supplied.]

We wish to point out that while certain grades of asbestos are used as a component part of some build-

ing materials, asbestos fiber itself is not a building material, and should not be classified as such. It is a *raw material* of innumerable uses in industry, as are many other metals and nonmetallic minerals which are granted allowances of 15 to 20 percent or more. [Italics supplied.]

#### BARITE

(Percentage depletion first allowed beginning with 1944)

Senate Hearings, 1943

(Senate Hearings, Revenue Act of 1943)

[1968] Statement of JOHN S. HALE, Jamestown, Tenn. \* \* \*

Mr. HALE, Mr. Chairman, and members of the committee; I represent two small mining companies in Tennessee, Jamestown, Tenn., and we mine barites, \* \* \*

\* \* \* We find it in residual clay formation, and it is in there in the form of sand and boulders and gravel, and we have to take it from those clay forms and *wash* it. Barites has a high specific gravity, and we separate it by a *gravitation process*. \* \* \* [Italics supplied.]

House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

[1] Statement of MALCOLM TARVER, representing the committee on taxation, barite industry of the United States.

[5] (The prepared statement referred to is as follows):

Statement of MALCOLM C. TARVER, representing the committee on taxation, barite industry of the United States in support of H.R. 1993, and H.R. 3624, Eightieth Congress, First Session, by Mr. GEARHART, of California.

#### MAINTENANCE OF BARITE MINING INDUSTRY ESSENTIAL TO NATIONAL DEFENSE

Barite has four principal uses: Oil well drilling mud; paints; chemicals; and glass. In war it is used in explosives, incendiary bombs, case-hardening airplane parts, primers for artillery shells, hydrogen-peroxide disinfectants, tracer bullets, signal flares, and other varied chemicals. \* \* \*

[6] PROFITABLE PRODUCTION CANNOT BE CONTINUED IF PRESENT AIDS TO PRODUCTION LAPSE

The cost of delivering a ton of barite from the Cartersville, Ga., area to the du Pont Co. at Newport, Del., is \$15, composed of production cost of \$8.51 per ton plus freight rate of \$6.49 per ton. Nova Scotia producers are delivering barite to the du Pont Co. at the following cost:

Ore.....	\$7.00
Duty.....	4.00
Ocean freight.....	3.00
Dock service.....	.75
Dock insurance, etc.....	.12
Railroad freight.....	.75
Total, Delaware.....	\$15.62

[7] SUPPORTING DATA—HISTORY OF BARITE MINING  
INDUSTRY

There are herewith next appended statements collating data derived from certain authorities therein stated, showing the imports of *crude and ground barite* in the United States for the years 1900-44, inclusive, and the production of barites in the United States for the years 1900-45 inclusive, with data included in the last-mentioned table as to production in the State of Georgia in most of these years, the statements referred to follow on the next succeeding pages. [Italics supplied.]

**BENTONITE**

(Percentage depletion first allowed beginning with 1947)

House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

Statement of Richard D. Saylor, Washington representative of National Lead Co., representing bentonite interests.

[66] Bentonite is a claylike substance which has been formed by the weathering or altering of volcanic ash.

[67] Bentonite occurs in deposits from a few inches to several feet thick.

The stratified deposits are worked by the usual stripping methods. The overburden is 7 to 30 feet thick and is removed by scrapers and tractors, sup-



plemented by power shovels on beds that are deeply covered.

In some places the usual underground mining methods are employed.

The major markets for bentonite have been developed in the foundry and petroleum industries.

Approximately 28 percent of the total output in 1945 was used for drilling mud, and the same percentage for foundries. A little over 25 percent was used for oil filtering and decolorizing the remainder.

The remainder in a variety of miscellaneous uses, including cement, chemicals, and paints.

New developments are taking place for its use in plastics.

In 1945, the total output was 573,998 short tons, having a value of approximately \$3,770,000.

Now, the margin of profit is small on a ton of bentonite. *In the crude form, bentonite sells for around \$2 to \$3 a ton. That has to be dried and processed and is then sold somewhere between \$7.50 a ton and \$16, depending upon the amount of purification and handling it has to go through. [Italics supplied.]*

[68] Statement of Hon. FRANK A. BARRETT, representative in Congress from the State of Wyoming.

Wyoming is the biggest producer of bentonite, as Mr. Saylor has just mentioned. It is a comparatively new industry in Wyoming and in the country. A number of young men have gone into that business in the past 5 years in our State.

We have several big operators. The National Lead Co., which Mr. Saylor represents, has a plant in our State.

The Wyadac Mining Co. has a big plant in the State, but this industry lends itself very well to small businesses, and within the last 6 months, two young men have invested \$100,000 in a plant and in the purchase of mines containing bentonite.

Now, inasmuch as the main use of bentonite is for drilling purposes around the oil fields, *we have a ready market in the Rocky Mountain area for practically all the bentonite that can be mined in the area.* (Italics supplied.)

[69] Statement of Hon. FRANCIS CASE, a Representative in Congress from the State of South Dakota.

Bentonite, of course, does not have exactly the same mining problems as those rock nonmetallies like feldspar and spodumene, but it is similar in its mining problems and its uses to barite, barite being used as in oil-drilling mud the same as bentonite is, and in the Bureau of Mines' reports at least you find bentonite classed along with ball clay when they are talking of the various clays and the commercial problems that you have with them.

Senate Hearings, 1950

(Senate Hearings, Revenue Revisions of 1950)

[447] Statement of LOUIS H. HEYL, Vice President and General Manager, the Wyodak Chemical Co., Cleveland, Ohio.

We are miners and processors of bentonite clay. Under section 114(b) of the Internal Revenue Code,

the mining and processing of bentonite clay is granted certain exemptions in the form of percentage depletion along with several other mineral products.

[448]

It is therefore a definitely established fact that trucking bentonite *to the processing plants where it must be dried, granulated, or ground, is a vital portion of the processing steps necessary to develop it to its "first commercially marketable product" stage; that is, in dried, ground, or granulated form and packed in bags.* [Italics supplied.]

Senator MILLIKIN. Your first step does not change the character of the deposit in any way?

Mr. HEYL. No; whatever; it just reduces the moisture.

Senator MILLIKIN. That is, cleaning it up, drying it, and putting it into a certain form?

[449] Mr. HEYL. That is correct.

\* \* \* The bentonite processing industry is a comparatively small business conducted by the following companies: The American Colloid Co., Baroid Sales Co., the Black Hills Bentonite Co., the Eastern Clay Products Co., and ourselves, the Wyodak Chemical Co.

\* We have letters from the four other producers stating that their *sales of bentonite, pulverized and in bags, amounted to from 93 to 99 percent of their total sales; that granulated bentonite in bags accounted for from 1 to 2 percent of their total and that the small remainder consists entirely of crushed and dried bentonite shipped to commercial grinders for further processing.* [Italics supplied.]

In our individual case,  $98\frac{1}{4}$  percent of our total production sold is *pulverized and packed in bags and*

1½ percent is granulated and packed in bags while the remainder, about one-quarter of 1 percent, is crushed and dried and is sold to others for final processing. [Italics supplied.]

Since the five producers listed above make up the entire bentonite industry and since such a small percentage is sold other than pulverized and packed in bags, or granulated and packed in bags, it is our logical contention that "the first marketable product" is bentonite, so processed and so packed. [Italics supplied.]

[450]

Senator MILLIKIN. So that from the time it leaves your processing plant you do not add anything to it?

Mr. HEYL. No, sir.

Senator MILLIKIN. But it would be useless unless you did process it in the way that you mention?

Mr. HEYL. Yes. That is true. But I believe we bear that out by proving that about 98¼ percent of the sales are the pulverized or granulated bentonite. Some prefer to have it granulated. It takes water a little more readily. [Italics supplied.]

Senator MILLIKIN. Could the driller of an oil well use your product if it were not processed?

Mr. HEYL. No; they could not. They have tried it, but can't use it until it is pulverized or granulated.

Senator MILLIKIN. Does the purchaser of your bentonite pay you from the processing plant? Or does he pay you from the mine?

Mr. HEYL. He pays for the material as finally processed, either pulverized or granulated.

Mr. CHAIRMAN. It is not marketable until you do that?

Mr. HEYL. No, sir, it is not.

**BORAX**

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[2887] Statement re extension of percentage depletion allowance to Borax, by American Potash and Chemical Corp., Searles Lake, Calif.

The purpose of this statement is to summarize the facts which support the extension to borax of the percentage depletion allowance which is now granted to a large number of so-called nonmetallic minerals by section 114(b)(4) of the Internal Revenue Code.

[2887] DESCRIPTION AND OCCURRENCE

Borax (tincal or tincalconate) is a natural compound found at the present time principally in California and Nevada. \* \* \* It is a white powder readily soluble in water, producing a faintly alkaline solution.

Borax is found in the state of nature in a considerable variety of forms, such as brines in prehistoric desert lakes and in various rocks or ores known as colemanite, rasorite, kernorite, etc. *In commercial or trade parlance it is the crude or unrefined commercially marketable product derived from the application of various ordinary treatment processes to these brines and/or ores.* An important secondary product, boric acid, is obtained by the reaction of borax to sulphuric acid. In certain desert lake brines in California, borax is found in conjunction with such minerals as potash, thenardite (sodium sulphate) and trona which



have previously been granted percentage depletion. The commercial value of the borax is largely determined by the boron oxide content. [Italics supplied.]

The Minerals Yearbook of the Bureau of Mines for the year 1947 contains the following data with respect to the production of boron minerals in the United States:

[2890]

Exact comparable data on domestic prices for borax for various years are not available, inasmuch as freight costs are a very substantial element in the cost to the user or consumer, and the practices of the industry with respect to freight absorption, quotation of delivered prices or prices f.o.b. mill have varied considerably. Notwithstanding deviations in some years, the general price trend has been noticeably downward. The January 1, 1949, price of American Potash & Chemical Corp. for borax in bags per ton f.o.b. Trona, with no freight allowance, with \$35.25 per ton, as compared with a price of \$151 per ton in 1920. Of this 1949 price, \$4 per ton represents charge for bags.

[The above statement was also presented at the Senate Hearings in 1951 (The Revenue Act of 1951, Hearings before the Committee on Finance, United States Senate, 82d Cong., 1st Sess., on H.R. 4473 (1951), p. 1060).]

#### CALCIUM CARBONATES

(See "LIMESTONE: ALL GRADES \* \* \*", *infra*, pp. 363-381)

## CLAM SHELLS

(See "SHELLS", *infra*, pp. 418-423.)

## CLAY: BALL

(Percentage depletion first allowed beginning with 1942)

Senate Debate, 1942

(88 Cong. Record (Part 6), 77th Cong., 2d Sess.)

[8021] Mr. McKELLAR. Mr. President, this amendment would put certain materials on the same basis as coal, oil, fluorspar, and other things which are given depletion allowances. Ball clay is used in making earthenware, various kinds of plumbing fixtures, and many other things which are useful both in the Army and Navy, and in the war effort generally, and also in our everyday life.

*The clay-mining company does no manufacturing. It sells to manufacturers of dishes for domestic use, such as \* \* \*. These dishes are the vitrified type, similar to those used in hotels. [Italics supplied.]*

Another important outlet for clay from the mines is the manufacturing of sanitary wares, plumbing fixtures, made by such firms as Standard Sanitary, Kohler, Crane, Universal, Sanitary Manufacturing Co., and others.

The particular kind of clay I am seeking to have covered is found in great quantities in the States of Kentucky, Tennessee, Missouri, and perhaps others.

[8023] Mr. BARKLEY.

Ball and sagger clay is a peculiar type of clay from which porcelain is made. \* \* \* In order to mine it the surface of the earth above it must be stripped away. \* \* \*

Ball and sagger clay is not the type of clay out of which ordinary earthenware vessels are made. It is a very highgrade, peculiar, special type of clay. The trade name is ball and sagger clay, which is well understood in the trade. It is a clay out of which a very fine type of porcelain is manufactured. *It is shipped from small clay mines or pits to factories where the porcelain is manufactured.* As I have already stated, much of it is now being used to manufacture insulation, which is necessary to the war effort. [Italics supplied.]

The clay pits are all owned by local interests. No large corporations own any of them. That fact has nothing to do with the merits of the case; but the corporations are all small and are owned by local interests.

Prospecting for this type of clay is done partly by machinery and partly by hand. The earth above the clay is removed, as in the case of a strip coal mine. The earth is moved away, and the clay is exposed so that it can be mined by machinery and shipped to factories.

House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

[63] Statement of F. L. CAROTHERS, Paris, Tenn., representing the Ball Clay Interests.

I come here to represent the seven principal producers of ball clay. Ball clay is a trade name given to a certain type of clay years and years ago.

It means a clay that is fine of texture, plastic, and when fired, burns to a white, attractive, or acceptable color.

Ball clay is used in making dishes. We use it on our tables, in bathroom fixtures, cooking utensils; it is used in floating enamels, making refractories necessary for the forming of glass, iron and steel, and many other things that are formed in high-temperature refractories.

Ball clay is used in all types of ceramic insulation.

It so happens that these seven companies produce every year from 94 to 96 percent of the ball clay that is produced in the United States, according to the figures compiled by the Bureau of Mines.

Now, I come here representing a rather odd industry. It is a rather small industry in dollar volume. It is a small industry in tonnage, and our prices per ton are comparatively low.

In 1940, the total dollar volume of ball clay produced in the United States was \$1,065,503.

Ninety-five percent of that material was produced in these western districts of Kentucky and Tennessee.

[65] Mr. CAROTHERS. The average price per ton in 1940 was \$7.37 for the entire industry. Some of our companies go 70 feet in the ground before they get any place.

In 1946, it was \$9.85.

Mr. CAROTHERS. *There is some clay exported from this country to South America. We exported a car the other day to Greece. [Italics supplied.]*

[66] Mr. SIMPSON. Mr. Carothers, you are speaking

only of a small amount of the clay consumed in this country, are you not?

Mr. CAROTHERS. Oh, yes. The ball clay is a very small part of the clay. In other words, that does not take in the clay that a brick house is made out of.

Mr. ELLIS. Mr. Carothers, all of what you term "ball clay" is not all the clay that goes into the manufacture of tableware, is it?

Mr. CAROTHERS. No, sir; China clay.

**House Hearings, 1950**

(House Hearings, Revenue Revision of 1950)

[441] Statement of E. A. GARBER, President, Harbison-Walker Refractories Corp., Pittsburgh, Pa.

Mr. GARBER. I not only represent Harbison-Walker, but over 50 refractories who produce about 90 percent of the refractory or fire material used in the United States. \* \* \*

[463] Mr. SIMPSON. Mr. Garber, your clay [refractory and fire clay] is distinguished from others we have heard of today, such as ball clay and sagger clay, is it? It can be distinguished from those clays?

Mr. GARBER. Yes, sir; due to the fact that it is used for an entirely different purpose.

**Senate Hearings, 1951**

(Senate Hearings, Revenue Act of 1951)

[915]

Statement of EDWARD J. GRASSMAN.

We were taken care of in the act of the Eightieth Congress, 1946 and there has been no change made,



so I am here to answer any questions you may wish to ask, but also on behalf of some of my friends in the ball and sagger clay industry. We would like to ask, on their behalf, that the wording of section 304 on the twentieth line—

Senator BUTLER. What page?

Mr. GRASSMAN. Page 85. We ask that the wording be changed. We want the "and" stricken from the twentieth line and a comma inserted, and then it will be the same as the existing legislation. The present legislation says, "ball, sagger, and china clay."

We are afraid that the Treasury Department may contend under the present wording "ball and sagger clay, china clay"—that unless it was both a ball and a sagger clay it might not be allowed depletion.

\* \* \* \* \*

**CLAY: BRICK AND TILE**

(Percentage depletion first allowed beginning with 1951)

*Senate Hearings, 1951*

(Senate Hearings, Revenue Act of 1951)

[1025]

\* \* \* \* \*

**ALBERHILL COAL AND CLAY Co.,**

*Los Angeles, Calif., July 3, 1951.*

In re percentage depletion allowance for clays.

Senator WALTER F. GEORGE,

*Chairman, Senate Finance Committee,*

*Senate Office Building, Washington, D.C.*

DEAR SENATOR GEORGE: On June 8, 1951, I wrote a letter to the Honorable Robert L. Doughton, chairman of the House Ways and Means Committee on the subject of technical clarification of the allowances for percentage depletion for brick and tile clay and

refractory and fire clay as provided in the new tax bill under consideration at that time. Mr. Doughton acknowledged receipt of my letter but it evidently arrived too late for the matter to be investigated and a change made in the tax bill.

As passed by the House of Representatives, the new tax bill allows percentage depletion of 5 percent for "brick and tile clay" and 15 percent for "refractory and fire clay". I assume the two different percentage figures have been used on the theory that "brick and tile clays" are more plentiful than "refractory and fire clays." The suggestion behind the wording used is that the end use of a clay shall determine the percentage grouping into which it shall fall.

The use of these terms does not make a definable grouping of clay products that can be segregated one from the other or is related to the supply of clay available for the manufacture of the products in either group. May I briefly illustrate these two points. First, the word "brick" includes firebrick as well as common brick. Firebrick are also refractories. Second, the word "tile" includes glazed bathroom tile as well as drain tile. Glazed bathroom tile are made from clays in relatively short supply and drain tile from clays that are plentiful. Further, many of the same clays are used in brick, tile, refractories and fire clay. For these reasons the end use yardstick of segregating clays for percentage depletion purposes will only create confusion in administering the law and will divide clays in a manner not related to scarcity or plentiful supply. It is conceivable that under the present wording of the proposed law the higher refractory clays made into many clay products would not be allowed any percentage depletion since on the face of it these clay products are not included in the definition of any of the clay products named.

I assume from the particular wording of the proposed bill that an attempt is being made to separate low grade clays that are mainly used for the manufacture of the class of low temperature fired clay products such as common brick and [1026] drain tile from the more refractory clays that are necessary for the manufacture of higher temperature fired clay products such as fire brick, face brick, flue lining, sewer pipe, conduit, pottery, glazed bathroom tile, etc.

Common brick and drain tile clays are sometimes mixed with the more refractory type of clays to manufacture some higher temperature fired clay products. Common brick and drain tile clay is generally a surface alluvial or adobe clay and is very common and plentiful in most parts of the United States. Large tonnages of this type of clay are used. The more refractory type of clays necessary for the manufacture of the higher temperature fired clay products are more rare and are only found in a limited number of localities. This type of clay is used in much less tonnage than the common brick and drain tile type of clay.

The easiest to define difference between these two types of clays is in their relative fusing temperature, that is the temperature at which the clays would fuse or melt. \* \* \*

I suggest in the proposed tax bill that the wording "Clays with a fusion point of the pyrometric cone equivalent of cone 5 or less" be used in place of "brick and tile clay" in the 5 percent depletion allowance group and "clays with a fusion point above the pyrometric cone equivalent of cone 5" be used in place of "refractory and fire clays" in the 15 percent depletion allowance group.

Use of either of the above definitions will not affect depletion allowances now provided for ball, sagger, and china clay. These three clays have a fusion point above the pyrometric cone equivalent of cone 5 and would fall in the 15-percent depletion group as under the present law.

Very truly yours,

CHAS. J. BIDDLE, *President.*

Copies mailed to Senators William F. Knowland and Richard M. Nixon and Mr. Colin Stam.

CLAY: CHINA

(Percentage depletion first allowed beginning with 1947)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[329]

The total sales of china clay in 1947 were only \$17,000,000. The average price received for china clay, as marketed in 1947, was \$12 per ton, f.o.b. mines. This is not the kind of nonmetallic mineral which the Treasury Department was referring to when it mentioned nonmetallic minerals costing 1 cent or less per ton in the ground.

Over half (54 percent in 1947) of the china clay produced goes into paper making. Clay imparts to paper opacity and a desirable finish and printing surface. Most paper used in printing contains some clay.

About 12 percent of china clay produced goes into rubber compounding. It is used in the manufacture of rubber to produce such products as rubber heels

and soles, rubber insulated wire and cable, jar rings, tires, plumbing supplies, doors stops, toys and a multitude of other products.

Another important use of china clay can be classified generally as use for ceramics, including refractory material, pottery and stoneware. These uses are well known and little purpose would be served in a further explanation.

\* \* \* \* \*

**CLAY: REFRACTORY AND FIRE**

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[441] Statement of E. A. GARBER, President, Harbison-Walker Refractories Corp., Pittsburgh, Pa.

Mr. GARBER. I not only represent Harbison-Walker, but over 50 refractories who produce about 90 percent of the refractory or fire material used in the United States. Next to agriculture, we probably are the second basic industry in the United States. Our products are used in every phase of industry where heat resistance is necessary.

\* \* \* \* \*

[442] Mr. GARBER. Coal, oil and gas, and many minerals, both metallic and nonmetallic, are granted percentage depletion in lieu of cost or discovery-value depletion under the existing provisions of the Internal Revenue Code. Among such minerals are ball, sagger, and china clay; bauxite; bentonite; and vermiculite.

However, refractory clays and quartzite are not granted percentage depletion, notwithstanding the following facts:

\* \* \* \* \*



(c) Most refractory clays are abstracted from the earth by underground mining methods similar to those employed in the recovery of coal. Some refractory clays and most refractory quartzite are recovered from open-pit mining operations, as are many metallic and nonmetallic minerals including ball, sagger, and china clay; bentonite; and most bauxite.

(d) Refractory clays have characteristics similar to ball, sagger, and china clay; bauxite; bentonite; and vermiculite, which are granted percentage depletion, and which have uses for refractory purposes.

\* \* \* "Refractory clay" is a term considered to include types of clay known as refractory flint, diaspore, and burley clays, bond or plastic clays, and kaolin. "Quartzite" is considered to include the rock sometimes called ganister. The locations of the areas within which deposits of refractory clays and quartzite occur, and the locations of plants in which refractory products are manufactured from refractory clays and quartzite, are shown upon the attached maps.

#### [449] Statement in Support of Percentage Depletion for Refractory Clays and Quartzite.

##### *Synopsis*

The following statement is made in support of the request of the refractories industry that percentage depletion be granted to the refractory minerals, refractory clays and quartzite, on the same basis as such depletion is granted to other nonmetallic minerals under section 114(b)(4) of the Internal Revenue Code. Refractory clays and quartzite are now granted depletion only on the basis of cost or discovery value, whereas other nonmetallic and metallic minerals have been allowed depletion at the rate of 15 percent of gross income.

This statement gives a discussion of the refractory minerals as the raw materials of the refractories industry, their description and occurrence, methods of mining, milling, and processing, statistics of the industry and the reasons why percentage depletion should be granted at the rate of 15 percent. [Italics supplied.]

From these data the discrimination in respect of percentage depletion, which presently exists against the producers of refractory minerals, is made clear and facts are furnished to show that every reason given in support of percentage depletion for the mineral products now covered exists in the case of the refractory minerals, and also, that from the standpoint of public policy and national defense, equal if not more urgent reasons exist for inclusion of the refractory minerals.

#### REFRACTORIES AND REFRACTORY MINERALS

##### *Refractories*

A list of the manufacturers of refractory products who may qualify for percentage depletion benefits is given as exhibit I. Pertinent statistics concerning the refractories industry are tabulated in exhibit II. The locations of the plants in which clay and silica refractories are manufactured are shown on the accompanying map of the United States, exhibit III.

##### *Refractory minerals*

There is no single descriptive word which may be used to name, without considerable definition, the minerals used in the refractories industry for the manufacture of refractories. The industry deems, however, that the phrase "refractory clays and quartzite" will

encompass such minerals without including deposits of clays and silica rock not used for refractories.

Chemically, refractory minerals must be pure. That is, they must be low in such impurities as iron oxide, lime or alkalis, which lower their melting points and render them useless for refractories. The term "refractory" modifying the words "clays and quartzite" has been suggested to embrace only the distinctively refractory minerals which fuse only at the highest temperatures. The terms "clay", "kaolin" and "quartzite," when used without the modifying term "refractory", include many materials having characteristics and properties which prohibit their use as refractories.

Several of these distinctively refractory minerals are already included among the minerals with respect to which percentage depletion is granted by existing law, viz, sagger clay, china clay, ball clay, and bauxite. [450] The following types of clay and silica-bearing rock are mined and used by the refractories industry, and those so used are considered to be embraced by the words "refractory clays and quartzite": Flint clay, including diaspore clay and burley clay; bond or plastic clay; kaolin; quartzite.

*The clays thus mined are sometimes also referred to as "fire clay" but this term also embraces clays which are not distinctively refractory minerals. Similarly, the term "quartzite" covers types widely used for purposes other than refractories. The refractory types, as stated, are chemically purer and melt only at the highest temperatures. [Italics supplied.]*

[453]

\* \* \* Among the materials granted percentage depletion in section 114(b)(4), those having characteris-

ties similar to refractory clay and in some cases having uses for refractory purposes are the following: sagger clay, bauxite, china clay, ball clay, bentonite, vermiculite.

[455]

#### THE PROPOSED AMENDMENTS

To provide percentage depletion for refractory clays and quartzite with respect to taxable years beginning after December 31, 1948, the following amendments to section 114 of the Internal Revenue Code are proposed.

4. Amend section 114(b)(4)(B) by inserting the words "refractory clays and quartzite" after the words "ball and sagger clay."

#### EXHIBIT I

*Manufacturers of refractory clay and silica refractories who may qualify for percentage-depletion benefits.*

[This list includes producers of more than 80 percent of the output of the industry.]

[This list contains the names of 67 manufacturers and the addresses of their refractory plants.]

[456]

#### EXHIBIT II

*Estimate of depletion allowance to manufacturers of clay and silica refractories based on percentage depletion of 15 percent.*

	Year 1947	Year 1948
Number of establishments (approximately) --	240	240
Manufactured value of refractory clay and silica products -----	\$137,000,000	\$165,000,000
Raw materials used (refractory clay and quartzite) :		
Tonnage (net) -----	5,400,000	5,200,000
Value -----	29,400,000	35,400,000
Estimated depletion allowance:		
(a) Basis:		
15 percent of value -----	4,410,000	5,310,000
Federal tax (38 percent) -----	1,675,800	2,017,800
(b) Basis:		
One-half of net income -----	3,025,000	3,328,000
Federal tax (38 percent) -----	1,149,500	1,262,000

Note.—(b) basis would apply, being less than (a) basis [Italics supplied.]

[463] Mr. SIMPSON. Mr. Garber, your clay is distinguished from others we have heard of today, such as ball clay and sagger clay, is it? It can be distinguished from those clays?

Mr. GARBER. Yes, sir; due to the fact that it is used for an entirely different purpose.

\* \* \* \*

Mr. SIMPSON. What is it used for, principally?

Mr. GARBER. *The products we manufacture* are used for linings in blast furnaces, open hearth, coke oven, cement kilns, chemical plants, anywhere where heat is necessary to produce a product. [Italics supplied.]

\* \* \* \*

Mr. JENKINS. You have three or four plants down in southern Ohio, down in my section.

Mr. GARBER. Yes, sir.

Mr. JENKINS. And your product comes out as regular bricks, does it not? You make bricks?

Mr. GARBER. We first mine the clay.

Mr. JENKINS. I know.

Mr. GARBER. Then we process it into bricks at high



temperatures. We burn the clay at high temperatures after forming.

[p. 464]

Mr. GARBER. I speak for 95 percent of the industry. That is right.

House Hearings, 1953

(House Hearings, General Revenue Revision (1953))

[2070] Statement of RUSSELL P. HEUER, Representing the Refractories Institute.

Mr. HEUER. My name is Russell P. Heuer. I am vice president of General Refractories Co., Philadelphia, Pa. I represent the Refractories Institute, a national association of 87 refractory manufacturers, and this statement is made in behalf of its members and the entire refractories industry. I wish to cite the benefits to the national economy which have been derived from the granting of the allowance for percentage depletion to refractory and fire clays and quartzite by the 1951 Revenue Act and to urge the retention of this provision in its present form.

The specific Internal Revenue Code provision to which I refer is section 114(b)4(A), which was amended by Congress in Public Law 183, 82d Congress, 1st session, by the addition of "refractory and fire clays, quartzite" to the minerals subject to percentage depletion.

MINERALS USED IN THE MANUFACTURE OF REFRACTORIES

*Refractory products are manufactured from carefully selected minerals, the chief minerals being refractory and fire clay and quartzite. The raw minerals are crushed, ground, and blended, and then made*

into brick and shapes for use in furnace construction. [*Italics supplied.*]

[2072] ADMINISTRATION OF THE ALLOWANCE OF PERCENTAGE DEPLETION OF REFRACTORY MINERALS

The refractory industry has generally adopted the view that "ordinary treatment processes" as that term is used in the Internal Revenue Code, section 114(b)4(B), includes in the term "mining," in the case of refractory and fire clays and quartzite, the process of crushing, grinding, screening, and blending of the raw minerals.

Regulations 111, section 29.23 (m)-1(f) as amended by the Treasury Department on July 14, 1953 are not inconsistent with the view of the industry.

The industry further believes that the attitude of its members as to the technical provisions relating to the computation of percentage depletion has been fair and reasonable. The industry, therefore, respectfully submits that the present percentage depletion provisions relating to refractory and fire clays and quartzite should be retained in their present form and urges your committee to adopt this conclusion in its consideration of possible amendments to the Internal Revenue Code.

COAL

(Percentage depletion first allowed beginning with 1932)

Senate Hearings, 1954

(Internal Revenue Code of 1954, Hearings before the Committee on Finance, United States Senate, 83d Cong., 2d Sess.)

[1409] Statement of W. BRICE O'BRIEN, Assistant Counsel, National Coal Association, accompanied by Lovell H. Parker, Chairman, Tax Committee.

Mr. O'BRIEN. Mr. Chairman, my name is W. Brice O'Brien. I am assistant counsel of the National Coal Association, representing bituminous coal producers throughout the Nation. I am accompanied by Mr. Lovell H. Parker, chairman of the association's tax committee.

\* \* \* \*

We are advocating, on behalf of the coal industry, four amendments to H.R. 8300—dealing with dust allaying and antifreeze treatment of coal, \* \* \*. However, because of time limitations, we will discuss here only the amendment dealing with dust allaying and antifreeze treatment of coal. We ask that our written statement, dealing in detail with all four recommendations, be made a part of the record of these hearings.

The CHAIRMAN. That will be done.

(The statement referred to follows Mr. O'BRIEN's testimony.)

Mr. O'BRIEN. In the decade beginning in 1930 dust-allaying treatment was developed on a broad scale to combat the alarming trend away from coal as a domestic fuel. This technique has been only partially successful, as evidenced by the fact that in the last 10 years the retail deliveries of bituminous coal have been cut almost in half. Nevertheless, if any part of the domestic market is to be retained, the coal which serves that market will have to be dust-treated. The industry is having an extremely difficult time selling coal to the householder even with dust treatment. If we must sell dusty coal, our job is utterly hopeless. Without dust-allaying treatment, it is prac-

tically impossible to sell coal for domestic heating purposes.

Section 114(b)(4)(B) was added to the Internal Revenue Code in 1943. This section provides a definition of gross income from the property, upon which percentage depletion is based. This definition is carried over in subsection (c) of section 613 of H.R. 8300.

Under the definition, "gross income from the property" means the gross income from mining. The provision specifies that "mining" includes not merely the extraction of the ores or minerals from the ground but also the "ordinary treatment processes" normally applied in order to obtain the commercially marketable product or products. The provision further specifies that ordinary treatment processes include the following:

In the case of coal—cleaning, breaking, sizing, and loading for shipment.

In *Black Mountain Corporation v. Commissioner* (21 T.C. No. 83), promulgated February 25, 1954, the Tax Court held—with Judge Arundell dissenting—that the application of a fine oil spray or mist to coal for the purpose of allaying dust is not an ordinary treatment process within the meaning of the statute. The Tax Court held, therefore, that the gross income from the property upon which percentage depletion is based must be reduced by the amount of gross income from the dust-allaying treatment and that the net income from the property which also provides a limitation on percentage depletion must be reduced by any profit involved in the dust-allaying treatment.

[1410] This decision was promulgated too late for us to bring this matter to the attention of the Ways and Means Committee. We ask, therefore, that this

committee amend subsection (c)(4)(A) of section 613 of H.R. 8300 to read as follows:

In the case of coal—cleaning, breaking, sizing, dust-allaying and antifreeze treatment, and loading for shipment.

The CHAIRMAN. Anti what?

Mr. O'BRIEN. Antifreeze.

The CHAIRMAN. Tell us about that.

Mr. O'BRIEN. When coal is shipped in the northern parts of the country during the winter months, it is necessary to use certain chemicals or other materials—I believe calcium chloride is the most common—when the coal is loaded on the car, to keep the coal from freezing in the car. Without such treatment in the cold months it would be very difficult to get the coal out of the car. It freezes I believe primarily in the corners of the car.

The CHAIRMAN. Is that a common practice?

Mr. O'BRIEN. It is.

The CHAIRMAN. What is the percentage of coal sold subjected to that practice?

Mr. O'BRIEN. It depends upon the weather at the time of shipment. If the weather is below freezing at the time of shipment, it is my understanding that all of the coal in that climate is treated for antifreeze. But coal shipped in the summertime, of course, is not so treated.

Unfortunately, I am unable to give you figures as to the percentage of the total production.

The CHAIRMAN. Well, is it a common practice?

Mr. O'BRIEN. It is, sir. It is universal.

The CHAIRMAN. All right.

Mr. O'BRIEN. With respect to the dust treatment, the Tax Court recognized, in the Black Mountain decision, the following important facts:



On the average, only 11 pounds of oil are applied to 2,000 pounds of coal, and the oil so applied does not add to the burning qualities of the coal in any measurable amount. In other words, the burning qualities of the coal are not benefited by the oil treatment. The purpose of the oil treatment is primarily and purely to allay the dust which would otherwise be so annoying to the householder.

The CHAIRMAN. What percentage of your coal is customarily subjected to that treatment?

Mr. O'BRIEN. In the last year for which figures were available—I believe that was 1949—some 41 million tons of coal were subjected to the dust-allaying treatment.

The CHAIRMAN. Out of a total of how much?

[1411] Mr. O'BRIEN. Out of a total of 465 million tons—approximately 9 percent.

The CHAIRMAN. You say it is about 9 percent?

Mr. O'BRIEN. Yes, sir. The point is, however, that that 9 percent of total production represents, as near as we can judge, somewhere over 90 percent of the coal which goes to the domestic home. Retail deliveries of coal in that year amounted to about 65 to 70 million tons. But retail deliveries include not only domestic coal, but includes also coal to the small industries and to the hotels and large apartment houses.

Now, much of that coal it is not necessary to dust treat. It is necessary to dust treat over 90 percent of the coal which goes into the home.

Government figures aren't available as to the exact percentage of home coal which is dust treated. The reason for that is that there is no breakdown in the amount of retail deliveries between homes and these small industries. Our sales people are convinced, however, that practically all coal that goes into the

home is dust treated and must be dust treated in order to be sold.

The CHAIRMAN. Do you have any evidence of that in the House?

Mr. O'BRIEN. The only evidence on the point was opinion evidence which was presented to the Tax Court in the Black Mountain case in Chicago. They made no specific finding in their decision as to the percentage of domestic coal which is oil treated or dust treated. There is no available evidence other than opinion testimony of expert witnesses.

The CHAIRMAN. Is the treatment done by the mines or by the distributor?

Mr. O'BRIEN. The treatment is done at the mine. The Tax Court recognized that it is not feasible for this dust treatment to be done anywhere other than at the mine, before shipment. Early in the game, in the 1930's, when this treatment first developed, some retailers did try to apply their own dust treatment.

[1413]

The CHAIRMAN. I want to ask you another question: How usual is this in the business?

Mr. O'BRIEN. Only 9 percent of the total production is dust treated, approximately 9 percent or 10 percent. However, over 90 percent of coal which goes into homes is dust treated. Now, practically every mine of any size, practically everything but the gopher hole, has dust treatment equipment. They use that dust treatment equipment and process only for the coal which goes into the home.

I should correct that statement: In some cases they use it for other types of coal. I believe certain types of slack are dust treated, so it won't all blow away

during shipment. But primarily it is used almost totally for coal which goes into the home.

DIATOMACEOUS EARTH

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[439] Statement of A. R. BOLLAERT, Vice President, Great Lakes Carbon Corp., New York.

[440] I am vice president and general manager of the Dicalite Division of Great Lakes Carbon Corp., who mine and process diatomaceous silica. I do not know whether many of you gentlemen know what diatomaceous silica is, and for your edification, a brief description would be that it is the siliceous skeleton or remains of marine plants or aquatic plants, inasmuch as it is found in both salt water and fresh water, from that origin.

For instance, we have vermiculite, feldspar, mica, talc, barite or sometimes called barites, china clay, and bentonite. Those materials are all *competitive to us* in one form or another, and inasmuch as these materials currently enjoy a percentage depletion under the Internal Revenue Code, we respectfully ask that the present discrimination be removed so that we can be truly competitive to these materials. [Italics supplied.]

[The above statement was also presented at the House Hearings in 1951 (Revenue Revision of 1951, Hearings before the Committee on Ways and Means,

House of Representatives, 82d Cong., 1st Sess.) (Part 3) (1951) p. 1649.]

#### DOLOMITE

(See, "LIMESTONE: ALL GRADES \* \* \* plus other stones, including dolomite, \* \* \*", *infra*, pp. 363-381.)

#### FLUORSPAR

(Percentage depletion first allowed beginning with 1942)

Senate Debate, 1942

(88 Cong. Record (Part 6), 77th Cong., 2d Sess.)

[8023] Mr. BARKLEY. \* \* \*

[8024] The Committee on Ways and Means included fluorspar in the depletion provision. Fluorspar is an absolutely indispensable *ingredient* in the manufacture of steel. It is produced in only a very few places. Ninety percent of it in the United States is produced in a little vein in southern Illinois and western Kentucky. \* \* \* [Italics supplied.]

Mr. HATCH. I ask unanimous consent to have printed in the Record at this point a résumé of some of the salient points in the fluorspar industry.

Mr. BARKLEY. I shall be very glad to have it in the Record.

There being no objection, the statement was ordered to be printed in the Record, as follows:

#### BRIEF RÉSUMÉ OF SALIENT POINTS IN THE FLUORSPAR INDUSTRY

General: The principal producing areas are western Kentucky and southern Illinois along the Ohio River. These two areas have pro-

duced 90 to 95 percent of the total fluorspar produced in the country. There are two types of deposits, the flat lying bedded deposits in the cave-in rock area of Illinois and the vein type of deposits in Illinois and Kentucky. In the West there is production in New Mexico, Colorado, Utah, and Arizona. Colorado and New Mexico seem to have the greatest possibility for increased production. All of this production is from vein types of deposits.

**Grades:** There are three grades of fluorspar. **Metallurgical grade** which has a minimum specification of 85 percent calcium fluoride, and a maximum specification of 5 percent silica. This material is used in the open hearth and electric steel furnaces and ordinarily the steel furnaces are unwilling to accept material which runs more than 15 percent fines. \* \* \*

The ceramic grade of fluorspar has a minimum specification of 96 percent fluoride, a maximum specification of 3 percent silica, and a maximum specification of 0.12 percent iron oxide. *This material must be finely ground and is sold to the enamel and glass industries. [Italics supplied.]*

The acid grade of fluorspar is the highest commercial grade with the exception of the optical grade. This grade has a minimum specification of 98 percent calcium fluoride and a minimum specification of 1 percent silica.

*This specification is also shaded down to 97 and 11/2. It is also sold in ground form to consumers who use it to make hydrofluoric acid from which a variety of other chemicals are manufactured. \* \* \* [Italics supplied.]*

**Prices:** Prices on all grades of fluorspar have been frozen as of the level existing on January 2, 1942. On the average, this means that the Illinois-Kentucky producers are receiving from \$24 to \$25 per short ton of metallurgical grade fluorspar, freight on board loading points. The



ceramic and acid grades are selling for from \$32 to \$34 per short ton. The western producers are handicapped by the amount of the freight from their mines to the Illinois-Kentucky area. In general, the price in New Mexico and Colorado for metallurgical grade is \$17 to \$18. The price of the acid grade ranges from \$27 to \$28.

\* \* \* \* \*

House Hearings, 1947

\* \* \* \* \*

(House Hearing, Percentage Depletion (1947))

\* \* \* \* \*

[19] Statement Concerning Making Percentage Depletion for Fluorspar Permanent.

\* \* \* \* \*

[20] Fluorspar is a hard, translucent, nonmetallic mineral that is found usually in veins and is mined through shaft and tunnels. In its pure form it is 51 percent calcium and 49 percent fluorine. It is a mineral which in color runs from white, light amethyst, canary yellow, bluish-green to deep purple. When ground for refining it is white with usually either a slight purplish or grayish cast.

*Fluorspar ores* are mined and milled by somewhat similar method to those employed for ores, such as those of the metals lead, zinc, and copper. Fluorspar deposits are found in about a dozen States. \* \* \* [Italics supplied.]

Fluorspar was used first as ornaments by the Indians but it soon found a place in smelting of ores because it aids in making the slag produced in smelting the ores of iron, copper, etc., more fluid. Thus, its principal single use, tonnagewise, has been and still is as a flux in the manufacture of basic open-hearth steel.

Fluorspar is produced and used in three grades, designated as:

\* \* \* \* \*

[A similar statement entitled "Statement of Illinois-Kentucky Fluorspar Producers Committee" was presented at the House Hearings in 1950 (Revenue Revision of 1950, Hearings before the Committee on Ways and Means, House of Representatives, 81st Cong., 2d Sess. (vol. 1) (1950), pp. 475-476).]

#### FULLER'S EARTH

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1618] Statement of CHARLES E. GLASSER, President, General Reduction Co., Chicago, Ill.

Mr. GLASSER. I am Charles E. Glasser, president of the General Reduction Co., Chicago, Ill. Our company mines fuller's earth at Macon, Ga. I respectfully request the adoption of a depletion of 15 percent of gross income for fuller's earth mining operations, or a percentage amount equal to that given many other similar nonmetallic clays and minerals.

Fuller's earth is a nonmetallic mineral in the form of a plastic-type *clay* used for the clarification of vegetable, animal, and mineral oils. It is also used in the formulations of agricultural insecticides and fertilizers, the treatment of municipal and other water supplies, sewage, and waste, as well as in many other miscellaneous chemical and physical applications which contribute to the national safety, health, and interest, both in peace and wartimes. [Italics supplied.]

A 15-percent depletion has already been allowed most metals and several nonmetallic minerals, includ-

ing certain clays. Based upon [1619] existing regulations we are unable to determine whether or not fuller's earth is classified as one of the other clay products which are somewhat similar in chemical analysis and mining hazards and which are now granted a 15-percent depletion allowance. If it cannot be so classified then it is our opinion that fuller's earth should be specifically given a comparable 15-percent depletion rate.

From a competitive end-use angle some of the clay products other than fuller's earth which now have a 15-percent depletion for mining operations are used in the manufacture of agricultural insecticides which are of utmost importance during our present war effort in order to produce agricultural foods so necessary for the national safety, health, and interest, and for the full war effort.

*Fuller's earth* is also widely used for this purpose. Thus, it seems only fair that no discrimination should be made and unless fuller's earth can be classified along with these other clay products, the former should be granted a specific 15-percent allowance for depletion. [Italics supplied.]

Although fuller's earth is a very important resource there are relatively few deposits of this material being mined in the United States and for this reason consumption by important essential industries is comparatively small. The industry is operated by very few companies having relatively small capitalization. \* \* \* In 1949 the Bureau of Mines reported only 320,906 short tons of *fuller's earth* sold at a value of \$5,199,642 for all producers. [Italics supplied.]

## GARNET

(Percentage depletion first allowed beginning with 1951)

Senate Debate, 1951

(97 Cong. Record (Part 9), 82d Cong., 1st Sess.)

[11724] *A. Percentage depletion*

\* \* \* \*

[12218] Mr. IVES. Mr. President, I send to the desk an amendment and ask that it be read and considered at this time.

The PRESIDING OFFICER. The clerk will state the amendment offered by the Senator from New York.

The CHIEF CLERK. On page 162, line 7, it is proposed to insert after the word "beryl" the word "garnet."

\* \* \* \*

Mr. IVES. Mr. President, I propose this amendment because of facts brought to my attention only a few days ago. The amendment would add garnet to those minerals granted depletion allowances under section 319(iii) of the committee bill.

Mr. James A. Barr, Chief of the Industrial Minerals Section of the Defense Minerals Administration, informed my office by phone on September 26 that the mineral called garnet was more-highly strategic from the point of view of national defense than any mineral presently granted depletion allowances under the committee bill. Mr. Barr emphasized garnet's strategic importance primarily because of the very limited supply available in the United States, and the almost complete absence of stockpiled reserves.

On the basis of this information, I urge that this amendment, which would grant a 15-percent depletion allowance for garnet, be agreed to. I am particularly concerned with this problem because over 90 percent of the garnet mined in the United States comes from the State of New York, believe it or not.

At this point in my remarks, Mr. President, I ask unanimous consent to have printed in the body of the Record a description of the garnet industry in New York published by the New York State Department of Commerce.

There being no objection, the matter was ordered to be printed in the Record, as follows:

#### GARNET

New York has large reserves of high quality garnet ore accessible for surface mining. While competition from garnet mines situated in other States, and in foreign countries, has been negligible, the garnet industry has operated under handicaps in recent decades due to the rise of manufactured competitive products. Among the most important of these artificial abrasives are aluminum oxide (fused alumina) and silicon carbide. \* \* \* Progress has been continuous in developing new methods of ore treatment and new forms of abrasive garnet. With such progress, the garnet industry will quite probably be able to compete successfully in many fields of abrasive requirements. *The mineral, garnet, is valuable because of its physical properties. Among the high grade natural abrasives, it ranks fourth in order of hardness, namely: diamonds, corundum, emery, garnet. \* \* \* [Italics supplied.]*

\* \* \* \* \*



[12219]

TABLE 16.—Abrasive garnet sold or used by producers, United States, 1900-1947

	Annual average	Annual average
	Short tons	
1947	8,722	814,071

Source: Minerals Yearbook.

TABLE 17.—Garnet, silicon carbide, and fused-alumina abrasives, average value per ton, selected years, 1920-48

	1920	1930	1940	1948
Abrasive garnet	\$79.33	\$82.79	\$84.90	\$73.64

1 Average value of output sold or used by producers in the United States.

Source: Minerals Yearbook.

## GRANITE

(Percentage depletion first allowed beginning with 1951)

(For granite other than dimension stone, see "LIME-  
STONE: All grades \* \* \* plus other stones, includ-  
ing \* \* \* granite \* \* \*," *infra*, pp. 363-381.)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[2890] Statement of National Building Granite Quarries Association.

The uses of granite are many—building material, bridge material, crushed stone for the construction and road-building industry. Approximately 50 percent of it is used in street curbing. In the North, it is indispensable in road building and street curbing, because severe cold weather disintegrates concrete. Granite used to be used extensively for post-office buildings and railway stations. For example, here in

Washington, Memorial Bridge and the Fourteenth Street Bridge, as well as the Old Post Office Building were constructed with granite. The "fines" or millings from the quarries and mills are extensively used in the poultry business for the feeding of poultry, the individual bird needing the grit. An estimated 150,000 tons per annum are sold for this poultry grit. Granite grits are preferable to any other in the poultry business. [*Italics supplied.*]

Senate Hearings, 1951

(Senate Hearings, Revenue Act of 1951)

[1059] Statement of RALPH A. FLETCHER on behalf of National Building Granite Quarries Association, Inc.

*Granite* is a natural resource, having been *commercially produced* in more than 75 percent of the States in the Union at one time or another. Although the material itself is common, deposits which are profitable to work under present conditions are not \* \* \* [*Italics supplied.*]

The Bureau of Mines reports that in 1949 there were only 139 active producers in the United States, although in 1928 the same Bureau reported 464 active units. This is not a case of fewer having more as is instanced by the volume used in rough construction which decreased from 356,000 tons in 1928 to 55,000 tons in 1949, while in the same period *dressed architectural granite* dropped from 1,400,000 cubic feet to 540,000 cubic feet. [*Italics supplied.*]

(Senate Hearings, Internal Revenue Code of 1954)

[1213] Statement of WESLEY E. DISNEY, Washington, D.C., representing the National Building Granite Quarries Association, Inc.

Mr. DISNEY. It is my pleasure to be here this morning. I represent the National Building Granite Quarries Association, Inc. You will recall that within recent years you gave granite 5 percent depletion. We are not squealing but we need some help.

At page 156 of the bill, at paragraph (f), we propose and hope the committee will adopt an amendment on this order, that—

In case of granite, limestone, marble, sandstone, slate, and other natural stones, ordinary treatment processes shall include any of the following: Sawing, grinding, cutting, polishing, and otherwise fabricating to dimension.

Our proposed amendment may include others who are not interested in it, in which event the committee may be at liberty, so far as we are concerned, to eliminate the words "limestone, marble, sandstone, and slate," so as to make the amendment read:

(f) In the case of granite and other natural stones, ordinary treatment processes shall include any of the following: Sawing, grinding, cutting, polishing, and otherwise fabricating to dimension.

The *uses of granite* are many. For example, it is used as a building material, bridge material, crushed stone for construction and roadbuilding, street curbing, poultry feed, monuments, and other uses. Building material, usually under architectural specifica-

tions, is required to be processed to form. Likewise bridge material. Street curbing must undergo a process to shape it for uniformity. One member of our association makes large quantities of slabs or markers for cemetery uses. These are required to be within certain specifications by the War Department. [*Italics supplied.*]

We are led to believe that the Treasury has the impression that the point at which percentage depletion begins is that point at which the rough blocks of granite are loaded on cars or trucks at the quarry, and the transportation to the processing mills will not be allowed, nor will the milling of the rough blocks be allowed. \* \* \*

[1214] There is a very good reason why this matter should be clarified by the Congress at this time. \* \* \*

[1215] In general, the types of equipment used and the types of treatment processes applied for a particular use, are similar throughout the industry. From these facts, it appears that the "gross income from the property" in the case of a granite producer is the gross sales of the product, whether sold in the form or grade for building material, bridge material, crushed stone for construction and roadbuilding, street curbing, poultry feed, or monuments, or for any other use. The statute does not contemplate nor require a producer to change or disturb its ordinary and usual business operations.

Senator CARLSON. You mention that little granite would be sold as quarried. That would apply to most stones, wouldn't it?

Mr. DISNEY. That is right. Most of our granite has to be processed in order to sell it, at all. For instance, street curbings here in Washington. If you

go anyplace in Washington, you will find granite. In our area, they are concrete, but here they are granite and they have to be processed. There would be no sale for it at all in crude blocks as it comes from the quarry.

The CHAIRMAN. *Don't they have establishments that do nothing but the final finishing of the granite?* [Italics supplied.]

Mr. DISNEY. *Yes.* For instance, one mill I have visited up in Massachusetts, they have a huge quarry and they get the granite out in huge chunks in rough form and then it is moved over there 2 or 3 miles to a mill that has all the modern sawing and polishing equipment. [Italics supplied.]

The CHAIRMAN. Is that mill owned by the quarry?

Mr. DISNEY. Owned by the same corporation, yes, sir. It is a part of it.

#### GRAVEL

(See "SAND AND GRAVEL," *infra*, pp. 413-416).

#### IRON ORE

(Percentage depletion first allowed beginning with 1932)

#### Senate Hearings, 1942

(Senate Hearings, Revenue Act of 1942)

[982] Statement of M. D. HARBAUGH, Cleveland, Ohio, Vice President and Secretary, Lake Superior Iron Ore Association.

\* \* \* \* \*

[985] Mr. HARBAUGH. If I understand your question, the commercial grades of iron ore at the present time average about 51½ percent iron.

Senator BROWN. Is it over 50 percent?

Mr. HARBAUGH. Yes.



Senator BROWN. Your low-bearing ores run around 35 to 38 percent?

Mr. HARBAUGH. They run upward of 30 percent and less than 40 percent. It is *necessary to concentrate that material*, of which there is an unlimited supply, in order to take the place of these commercial grades of ore which heretofore we have been able to mine by open-pit methods very simply and rapidly. If we had not had these open-pit ores at the present time for this war emergency, I do not know what we would have done, because it is *mainly these mines that have been able to account for this very rapid expansion of output.* [Italics supplied.]

\* \* \* \*

[987] Senator DANAHER. What do you consider that word "representative" to mean, or what standard do you apply to decide whether it is a representative normal market price?

Mr. HARBAUGH. *The price of iron ore is a generally well known figure, a published figure. These operating companies that turn over their ore to the owners, operate at cost; they are not profit companies, you see, and therefore some market price would have to be established to determine what is a fair profit in that case. In other words, there is no profit in the transaction as it is now recorded. It will be up to the Commissioner undoubtedly to determine what was the current, normal price, which could be easily determined from just the general published information about the industry.* [Italics supplied.]

\* \* \* \*

## (Senate Hearings, Revenue Revisions of 1950)

[299] Statement of M. D. Harbaugh, Vice President, Lake Superior Iron Ore Association, Cleveland, Ohio.

\* \* \* \* \*

[301] Section 204(c) of the bill, regarding percentage depletion, in revising the definition of gross income from mining, would create a deterrent that certainly will adversely affect the development of *low-grade ores* including the *taconites, which require beneficiation*. Plants cannot always be established directly at the property \* \* \*. [Italics supplied.]

Senator MILLIKIN. How far would you carry the transportation cost?

Mr. HARBAUGH. Well, we have plants that are located several miles from the source of the ore, centralized plants which are necessarily large in which ores from numerous small pits or small workings can be treated.

Senator MILLIKIN. How do you treat the iron ore at those smaller plants?

Mr. HARBAUGH. The ore is treated in these plants by *washing* to remove some of the [impurities] and by *other concentration processes* such as are technically known as jigging and heavy density separation. [Italics supplied.]

Senator MILLIKIN. You are simply preparing the ores for the plant?

Mr. HARBAUGH. Yes, sir. *This part that is treated would not be marketable without this treatment.* [Italics supplied.]

Senator MILLIKIN. You would not run your cost down to Pittsburgh?

Mr. HARBAUGH. No. *This involves the transportation to the processing plant where we make the first marketable product.* [Italics supplied.]

Senator TAFT. And a product which can be shipped on boats?

Mr. HARBAUGH. Which can be shipped on boats and which is usable in the premises.

\* \* \* \* \*

**LIMESTONE: ALL GRADES (CALCIUM CARBONATES, METALLURGICAL AND CHEMICAL GRADE) PLUS OTHER STONES, INCLUDING DOLOMITE, GRANITE, MARBLE, AND SANDSTONE**

(Percentage depletion first allowed, beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[480]

\* \* \* \* \*

Statement of Russell Rarey, President, Marble Cliff Quarry Co., Columbus, Ohio.

Mr. RAREY. I would like to have about 5 minutes, if I may. We operate a limestone open quarry near Columbus, Ohio, and in the western part of the State a limestone underground mine. The quality of this stone we produce is such that it is marketed for chemical and metallurgical purposes, for burned lime, for agricultural use, for [481] railroad ballast, highway construction and maintenance, for building construction, and for various manufacturing and miscellaneous uses.

As a member of the executive committee and of the percentage depletion committee of the National Crushed Stone Association, *I have been authorized, along with Mr. Krause, to present a statement on behalf of the National Crushed Stone Association, and*

*the Agricultural Limestone Institute.* [Italics supplied.]

With your permission, Mr. Chairman, we would now like to file this formal statement for your consideration, and if I may I would like to emphasize the following few points.

The CHAIRMAN. Without objection, that will be done.

(The statement referred to follows.)

Statement in support of a percentage depletion allowance for producers of crushed stone.

(Prepared by National Crushed Stone Association and Agricultural Limestone Institute)

*Crushed stone* plays a vital part in the health and economic welfare of the Nation in both peace and war. The same or similar problems are encountered in the extracting, processing, and marketing of *crushed stone* as are encountered in the case of those minerals now granted a percentage depletion allowance, and for the same reasons encouragement for prospecting and development should be extended to *crushed stone* producers. In addition, some of those minerals to which percentage depletion applies are in direct competition with *crushed stone*. This statement is in support of a request for a 15-percent percentage depletion allowance for producers of *crushed stone*. [Italics supplied.]

#### FOREWORD

This statement was prepared and is presented by the National Crushed Stone Association and the Agricultural Limestone Institute, a division thereof, which represent producers of a substantial majority of *all the crushed stone* commercially mined and quarried in the United States. It is offered for the following purposes:

1. To present a brief but clear picture of the *crushed-stone industry* and its importance in the general industrial field, the place it occupies in the category of natural-resource industries of the United States, and the similarity of its geological occurrence and methods of recovery to certain other natural-resource industries to which percentage depletion allowances have been granted. [Italics supplied.]

2. To point out the inequitable and unjust discrimination which now exists against the *crushed-stone industry* by reason of its present exclusion from the list of natural resources enjoying the benefits of percentage depletion. [Italics supplied.]

3. To request a remedy for this situation by amendment of the Internal Revenue Code to extend the percentage depletion allowance of 15 percent of gross income to the *crushed-stone industry*. [Italics supplied.]

The principle of percentage depletion has been before Congress for so long and the soundness and equity of this method of arriving at depletion allowances have received such a thorough and technical consideration that this statement will not attempt to cover the same ground again but will only briefly refer to the principle to show its applicability to *crushed-stone production*. (See appendix.) [Italics supplied.]

#### DESCRIPTION AND USES

*Crushed stone includes* igneous rocks such as *granite*, *syenite*, *diorite*, *basalt*, and other trap rocks; sedimentary rocks such as *limestone*, *dolomite*, and *sandstone*; and metamorphic rocks such as *gneiss*, *schist*, *eclogite*, and *marble*. [Italics supplied.]

*Crushed stone is used for* concrete aggregate and road metal, metallurgical stone (flux), agricultural and ground limestone, railroad ballast, alkali works,



riprap and jetty stone, refractory stone, stone sand, and for a wide variety of miscellaneous uses. [Italics supplied.]

[482] *Highway construction*

By far the largest single use of *crushed stone* is for highway construction. \* \* \* [Italics supplied.]

*Agricultural limestone*

One of the important classifications of *crushed stone*, the use of which warrants special mention, is that of agricultural limestone, because of its effect on the health and economy of the Nation. \* \* \* [Italics supplied.]

PRODUCTION AND VALUE

*Crushed stone* is substantially produced in over 30 of the 48 States, with the States producing the largest tonnages being California, Illinois, Indiana, Iowa, Kentucky, Michigan, Missouri, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia, and Wisconsin. [Italics supplied.]

The latest statistics available, compiled by the United States Bureau of Mines for the year 1948, show a total of 223,863,780 short tons produced in the United States, with a value of \$280,960,452, making the average value per ton \$1.26. As can readily be seen, *crushed stone* sells at an extremely low price. High transportation and operation costs, together with the low sales price, leave the producer only a relatively narrow profit margin. \* \* \* [Italics supplied.]

MINING AND PROCESSING

[483]

The various types of stone in their natural occurrence and methods of recovery, in most respects, are similar to other minerals. They are found depos-

ited in different states of purity in beds or veins in the earth, and are recovered either by open pit or underground mining. \* \* \*

#### WHY CRUSHED-STONE PRODUCERS SHOULD BE ALLOWED PERCENTAGE DEPLETION

The producers of numerous minerals now enjoy this simplified method of returning capital to the taxpayer (see appendix), including direct competitors of the *crushed-stone industry*. \* \* \* [Italics supplied.]

#### DISCRIMINATION BETWEEN CRUSHED-STONE PRODUCERS AND OTHER MINERAL PRODUCERS

We heartily favor the percentage depletion method for other mining industries, but the *crushed-stone industry* fails to see any essential difference between the mining of crushed stone and certain nonmetallic minerals and is convinced that the discrimination between *crushed stone* and other nonmetallic minerals which have long had percentage depletion should be eliminated. [Italics supplied.]

[487] Mr. RAREY. The *crushed stone industry* requires the benefit of percentage depletion to remove the inequalities that now exist to its disadvantage. Materials such as rock asphalt for paving purposes, tar as a byproduct from coal, asphalt as a byproduct from oil, now benefit from percentage depletion, and all are competitive in the highway field with *crushed stone*. A similar inequality exists in many chemical and manufacturing processes where stone is competitive with other materials which now enjoy percentage depletion. [Italics supplied.]

It follows, therefore, that the *inequalities* that are said to now exist in the percentage depletion tax

structure in favor of the big corporations can and should be removed by making percentage depletion [488] available to small business as characterized by the members of the crushed stone industry. [Italics supplied.]

Mr. JENKINS. Let me ask you this question. I see you are the president of the Marble Cliff Quarry Co. there in Columbus.

Mr. RAREY. That is right.

Mr. JENKINS. What do you take out of your quarries, is it lime or sandstone?

Mr. RAREY. Limestone.

Mr. JENKINS. Altogether limestone?

Mr. RAREY. Yes, sir.

Mr. JENKINS. And your principal product is sold as crushed lime?

Mr. RAREY. Our principal product is metallurgical stone for the production of pig iron and for the burning of lime which in turn is used in part by the steel industry. We produce a great deal of road stone and railroad ballast and a considerable amount of ground stone for agricultural uses, particularly in the southern and southeastern part of the State.

Mr. JENKINS. In other words, in the manufacture of iron, all of the iron furnaces must have lime.

Mr. RAREY. It takes about 800 pounds of stone to a ton of steel.

Mr. JENKINS. You supply that as they want it.

Mr. RAREY. Yes.

Mr. JENKINS. It must have a certain chemical quality?

Mr. RAREY. It must have a certain chemical analysis.

Mr. JENKINS. Up to a standard.

Mr. RAREY. Yes.

Mr. JENKINS. You say there are many people in the country engaged in this business?

[489] Mr. RAREY. Not that particular type of business. *I speak for the crushed stone industry generally.* It goes into highways and construction, but there are subdivisions. You will recall that Mr. Dickey of the Kelley Island Lime & Transport Co. and the professor from Lansing, Mr. Landes, I believe it was, spoke earlier and directed their remarks specifically to the stone that is burned or can be burned. [Italics supplied.]

Mr. JENKINS. I presume that the big iron and steel companies like Republic and United States Steel have their own mines, do they?

Mr. RAREY. Some of them do. United States Steel Corp. does; Republic not so extensively. They buy considerable of their fluxing stone. We supply the independent furnaces, such as the American Rolling Mill, Wheeling Steel & Iron, and Timken.

Mr. JENKINS. All of these little foundries, and anybody that melts iron, they have to have that.

Mr. RAREY. They have to have a chemical stone of a given chemical analysis.

Mr. SIMPSON. If the committee should see fit to grant this allowance to your industry, *you would not want it confined to the metallurgical stone, stone used for metallurgical purposes?* [Italics supplied.]

Mr. RAREY. No; *I speak for the entire stone industry today.* [Italics supplied.]

\* \* \* \* \*

Statement of HORACE C. KRAUSE, President, Columbia Quarry Co., St. Louis, Mo.

Mr. KRAUSE. My name is Horace C. Krause, president of the Columbia Quarry Co. I am chairman of the percentage depletion committee for the National

**Crushed Stone Association and Agricultural Limestone Institute.**

Our company is operating three plants in Illinois and one in Missouri. Some of these plants are operated as open quarries, and some as underground mines. \* \* \* Our products are used in the following industries: Construction, farming, aluminum, pig iron, gray iron, glass, copper, lead, feed, minerals, fertilizers, clay pigeons, rubber, coal, roofing, explosives, chemicals, and other uses.

Other *limestone and crushed stone producers* supply materials that go into these industries: Carbide, soda ash, paper, pharmaceuticals, carriers and extenders, in paint, putty, remedies, chalk, whiting, and so forth. [Italics supplied.]

[490] We, therefore, ask that the *crushed stone industry, including limestone and stone of all types*, be granted percentage depletion. [Italics supplied.]

Mr. JENKINS. Mr. Rarey, who testified a little while ago, asked to have consent to file his written statement with his other statement.

[The same statement was again presented by Mr. Krause in Senate Hearings in 1951. See the Revenue Act of 1951, Hearings before the Committee on Finance, United States Senate, 82d Cong., 1st Sess., on H.R. 4473 (Part 2) (1951), pp. 902-908.]

Senate Hearings, 1950

(Senate Hearings, Revenue Revisions of 1950)

[808] Statement in support of Percentage Depletion for Crushed-Stone Producers.



## FOREWORD

This statement was prepared and is presented by the National Crushed Stone Association and the Agricultural Limestone Institute, a division thereof, which represent *producers of a substantial majority of all the crushed stone commercially mined and quarried in the United States.* \* \* \* [Italics supplied.]

## DESCRIPTION AND USES

*Crushed stone* includes igneous rocks such as *granite*, *syenite*, *diorite*, *basalt*, and other trap rocks; sedimentary rocks such as *limestone*, *dolomite*, and *sandstone*; and metamorphic rocks such as *gneiss*, *schist*, *eclogite*, and *marble*. [Italics supplied.]

*Crushed stone* is used for concrete aggregate and road metal, metallurgical stone (flux), agricultural and ground limestone, railroad ballast, alkali works, riprap and jetty stone, refractory stone, stone sand, and for a wide variety of miscellaneous uses. [Italics supplied.]

[809]

## PRODUCTION AND VALUE

The latest statistics available, compiled by the United States Bureau of Mines for the year 1948, show a total of 223,863,780 short tons produced in the United States with a value of \$280,960,452, making the average value per ton \$1.26. As can readily be seen, crushed stone sells at an extremely low price. High transportation and operation costs, together with the low sales price, leave the producer only a relatively narrow profit margin. \* \* \*

# WHY CRUSHED-STONE PRODUCERS SHOULD BE ALLOWED PERCENTAGE DEPLETION

The producers of numerous minerals now enjoy this simplified method of returning capital to the taxpayer (see appendix), including direct competitors of the *crushed-stone industry*. \* \* \* [Italics supplied.]

## [811] WHY THE RATE SHOULD BE 15 PERCENT

\* \* \* The percentage depletion method with an allowance of 15 percent of gross income has proved satisfactory in the case of similarly situated industries, such as rock asphalt, rock phosphate, potash, and ball and sagger clay, and has been easily administered at a minimum of cost to both the Government and the taxpayer. *Crushed-stone producers* believe that such an allowance would be eminently fair and as effective in their own case and respectfully request that your committee recommend to Congress an amendment to section 114 of the Internal Revenue Code which will extend the percentage depletion allowance of 15 percent of gross income to the producers of crushed stone. [Italics supplied.]

Respectfully submitted.

NATIONAL CRUSHED STONE ASSOCIATION,

By J. R. BOYD,

*Administrative Director.*

AGRICULTURAL LIMESTONE INSTITUTE,

By HENRY A. HUSCHKE,

*Managing Director.*

## (House Hearings, Revenue Revision of 1951)

[1631] Statements of RUSSELL RAREY, President, Marble Cliff Quarries Co., Columbus, Ohio, and HORACE C. KRAUSE, President, Columbia Quarry Co., St. Louis, Mo.

Mr. RAREY. Mr. Chairman, my name is Russell Rarey, of Columbus, Ohio. I am president of the Marble Cliff Quarries Co.

Our company operates a limestone open quarry near Columbus, Ohio, and a limestone underground mine in western Ohio. The character of the stone is such that it is used for chemical and metallurgical purposes, for burned lime, for agricultural use, for railroad ballast, for highway construction and maintenance, and for miscellaneous building purposes including airport runways, and so forth.

I am a member of the executive committee of the National Crushed Stone Association and also a member of its committee on percentage depletion. In this latter capacity, it was my privilege last year, along with others, to appear before your committee and submit a statement in support of percentage depletion allowance for the crushed stone and agricultural limestone industries.

[1632] Later your committee recommended that our industries be granted a percentage depletion allowance, and I assure you that the favorable recommendation of your committee was greatly appreciated by the members of our industry. Nevertheless, due to subsequent developments, those recommendations were not incorporated into law; we thereby continue without a percentage depletion allowance which is so badly needed.

In cooperation with Mr. Horace Krause, represent-

ing the Agricultural Limestone Institute, I wish to present for your consideration and for the record a formal statement on behalf of the National Crushed Stone Association and the Agricultural Limestone Institute.

This statement submits that the same reasons that won your favorable recommendation last year are as of this moment more impelling than ever before. May I commend the statement to you for your consideration. May I, also, with your permission, comment briefly as to these further impelling reasons.

Failure to grant to the *crushed stone industry* a percentage depletion lies in the difficulty of finding replacement areas for our exhausted stone deposits. \* \* \* [Italics supplied.]

[1633] Your committee was correct in its judgment of 1 year ago in recommending a percentage depletion allowance for the *crushed stone industry*, and there is now even greater reason why that judgment by your committee should be reaffirmed and we respectfully request your favorable consideration to that end. [Italics supplied.]

(The formal statement of the National Crushed Stone Association and Agricultural Limestone Association follows:)

Statement in Support of the Action of the Ways and Means Committee and the House in 1950 Approving Percentage Depletion for Crushed Stone.

*Producers of crushed stone* are fully aware that at first glance the addition of crushed stone to the depletion list appears inconsistent with the present need for revenue. However, in the first place, the revenue involved in this item is relatively inconsequential and, secondly, the need for revenue, however pressing, is

not a valid basis for an inequitable distribution of the tax burden so as to discriminate between *crushed stone* and competing nonmetallic minerals. [Italics supplied.]

[1634] In order to avoid repetition of evidence heretofore furnished the committee, we refer to the testimony on this subject given last year, which contains a fully documented discussion of the position of the *crushed-stone industry* in this matter (hearings, vol. 1, Feb. 9, 1950, pp. 480-491). [Italics supplied.]

We do however, hold strongly to our previous position that the allowance should be 15 percent as now accorded rock asphalt, ball and sagger clay, china clay, bentonite, vermiculite, iron ore, lead, zinc, and barite, all of which are directly competitive with crushed stone and agricultural limestone; and as accorded potash, phosphate rock, and trona, which are indirectly competitive. \* \* \*

The reasons which justified the committee and the House in voting last year to grant a percentage-depletion allowance to *crushed stone* are even more persuasive at this time in view of the increased tax burden, a fair share of which the *crushed-stone industry* will gladly assume in the interest of the defense program. [Italics supplied.]

NATIONAL CRUSHED STONE ASSOCIATION  
AND AGRICULTURAL LIMESTONE INSTITUTE,

RUSSELL HAREY,

HORACE C. KRAUSE,

*Members of Percentage Depletion Committee.*

MARCH 5, 1951.



[1635] Mr. KRAUSE. My name is Horace C. Krause, president of the Columbia Quarry Co., St. Louis, Mo. I am chairman of the Percentage Depletion Committee for the National Crushed Stone Association and the Agricultural Limestone Institute.

Our company is operating three plants in Illinois and one in Missouri. Some of these plants are operated as open quarries and some as underground mines. These plants produce riprap, derrick stone, agricultural limestone, ballast, fluxing stone, chemical limestone, crushed stone, and various types of fillers.

[1636] Mr. SIMPSON. *Are you referring to limestone used in agriculture, and also to crushed limestone used in construction work?* [Italics supplied.]

Mr. KRAUSE. *All purposes.* [Italics supplied.]

Mr. SIMPSON. What you object to is what appears to be a type of advantage to your competitors?

Mr. KRAUSE. That is correct.

Senate Hearings, 1951

(Senate Hearings, the Revenue Act of 1951)

[891] Statement of RUSSELL RAREY, President, Marble Cliff Quarries Co.

I wish to submit for the record this formal statement on behalf of the National Crushed Stone Association and Agricultural Limestone Institute in support of a percentage depletion allowance for the *crushed stone industry*, and I will not impose upon the time of the committee to read the statement, copies of

which, I understand, have been placed before you.  
[Italics supplied.]

The CHAIRMAN. You may put it into the record.

Mr. RAREY. Thank you, sir.

I do, however, desire to make the following observations in my own behalf in support of the formal statement.

My company operates a limestone open quarry or mine near Columbus, Ohio, and a limestone underground mine in western Ohio. The character of the stone is such that it is of value for chemical and metallurgical purposes, for burned lime, and for agricultural use, for railroad ballast, for highway construction and maintenance and for miscellaneous construction work, including airport runways, et cetera.

[892]

At this point may I suggest that a continuation of the *crushed stone business* is essential. Without suitable aggregates, there can be no modern construction; without agricultural limestone the productive capacity of our farm land would be reduced and our food supply lessened, and without metallurgical stone and lime, there can be no steel. [Italics supplied.]

[893]

Mr. RAREY. Well, with us we are in the Devonian stone in the Columbia and Delaware formations, which are limestone, with a high percentage of calcium and relatively low percentage of magnesium.

Roughly divided into general stratas, the upper ledges contain silica that makes it unsuitable for

chemical purposes, yet it is desirable for construction purposes; and the lower ledges are the chemical ledges that go into steel and lime, and the general chemical manufacturing processes.

Senator KERR. And which geological age, generally, provides the more abundant—

Mr. RAREY. I would not at this time be able to answer that.

Senator KERR. Opportunity.

Mr. RAREY. I would not know which geological formation or age—the common designation of those stones, such as granite or trap rock, as differentiated from limestone, each occur in different sections of the country, and *are each applicable to their own particular uses, although there is a common use, or there is a use that is common to all of them and that is in the construction field.* [Italics supplied.]

\* \* \* \*

(The prepared statement referred to follows:)

[894] Statement in Support of House Bill Provision to include Crushed Stone among Competing Minerals allowed percentage depletion.

In 1950, and again this year, the House has voted to eliminate an unjust discrimination against *crushed stone* and has included it among nonmetallic minerals entitled to percentage depletion. [Italics supplied.]

Last year the Senate Committee did not deny that *crushed stone* is entitled to percentage depletion, but decided "to postpone action on these proposals until your committee can carry out a more careful analysis of the problems involved." [Italics supplied.]

We urge this structural change in the act as a matter of equity. In fact, the House bill offers only partial relief since it provides a 5 percent depletion allowance for crushed stone, whereas certain compet-

ing minerals are granted 15 percent under existing law.

The competitive relationship between rock asphalt and *crushed stone* is such that failure to grant the same percentage depletion allowance of 15 percent to the *crushed stone industry* as is now enjoyed by the rock asphalt industry would be to continue an unjust discrimination. [Italics supplied.]

[895] For reasons set forth above we respectfully urge the committee to adhere to the position that it took last year of granting a percentage depletion allowance to *crushed stone* to remedy the discriminatory exclusion of *crushed stone* from the competitive minerals which are permitted depletion allowances. [Italics supplied.]

We do, however, hold strongly to our previous position that the allowance should be 15 percent as now accorded rock asphalt, ball and sagger clay, china clay, bentonite, vermiculite, iron ore, lead, zinc, and barite, all of which are directly competitive with crushed stone and agricultural limestone; and as accorded potash, phosphate rock, and trona, which are indirectly competitive. \* \* \*

#### House Hearings, 1953

(House Hearings, General Revenue Revision (1953))

[2100] Statement in Support of Percentage Depletion for Crushed Stone Producers by National Crushed Stone Association, Washington, D.C.

Mr. Chairman and gentlemen, my name is Russell Rarey and I am president of the Marble Cliff Quarries Co. at Columbus, Ohio, and I am chairman of the percentage depletion committee of the National

Crushed Stone Association. This statement is presented today on behalf of that association.

The National Crushed Stone Association reaffirms its belief in the long-recognized congressional policy that allowances for the depletion of natural resources should be determined on the basis of a percentage of gross income, and in the application of this policy to the stone industry.

#### INEQUITIES CREATED BY MULTIPLE RATES FOR THE STONE INDUSTRY

One of the basic reasons for percentage depletion was that the previous depletion system was " \* \* \* neither simple in its application nor equitable in its results. The \* \* \* system \* \* \* [was] not only inequitable between taxpayers in the same branch of the mining and quarrying industry, but the distribution between the different branches \* \* \* [was] unjust." Staff Report on Depletion, Joint Committee on Internal Revenue Taxation, 1929, p. 22).

(a) *Discrimination between the stone industry and its competitors.*—When this association appeared before your committee in 1951 we adhered to our prior request for a uniform rate as follows:

\* \* \* \* \*

We now reaffirm this position and recommend adoption of a 15-percent uniform rate for the stone industry.

(b) *Discrimination between members of the stone industry.*—The Revenue Act [of 1932] which followed the joint committee report of 1929, cited above, fixed a uniform percentage depletion rate of 15 percent for all metal mines. The revenue bill of 1949, as it passed the Senate, added stone to the percentage depletion provision at 15 percent for all quarries.



These Senate-approved additions, including the flat 15 percent rate for all stone deposits, were postponed when the bill went to conference.

As the Revenue Act of 1951 was finally enacted it contained three different rates for stone: 15 percent for limestone, chemical grade and metallurgical grade; 10 percent for calcium carbonates, magnesium carbonates, and dolomite; and 5 percent for stone. *Stone in all of these categories in many instances is quarried by the same company, and in some instances from the same quarry.* [Italics supplied.]

It is apparent, therefore, that *with three rates of percentage depletion applied to the product of our industry* inequalities of tax treatment exist as between different and competing individual members of our industry. Establishment of a uniform rate of 15 percent for all of the products of our industry would not only cure this defect but also resolve numerous administrative problems these inequalities create. [Italics supplied.]

#### **LIMESTONE: ONLY CHEMICAL AND METALLURGICAL GRADE**

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[332] Statement of Ralph L. Dickey, President, the Kelley Island Lime & Transport Co., Cleveland, Ohio.

Mr. DICKEY. My name is Ralph L. Dickey. I am president of the Kelley Island Lime & Transport Co. of Cleveland, Ohio. I am appearing as a representative of a committee of the National Lime Association requesting a 15-percent depletion allowance for limestone when calcined or when used by the metal-

lurgical or chemical industry. A [333] bill, H.R. 2537, has been introduced and is pending before this committee which would accomplish this result. Our company operates three quarries in Ohio, two of which have adjacent calcining lime plants, and one lime plant at Buffalo, N.Y.

The types of high quality limestone used for metallurgical or chemical purposes or for producing calcined products are found in relatively few areas and constitute an insignificant proportion of all limestone deposits. This bill provides depletion allowance for only such high grade limestone that is produced for the uses described.

Under present highly competitive conditions, fuel and labor costs, and greatly increased plant investments required, any limestone deposit which is used for the calcination or burning of lime must be of high chemical purity. The term "limestone when calcined" includes all forms of burnt lime, *including burnt dolomite*. [Italics supplied.]

\* \* \* \*

[334] As to possible difficulties in administration, it is a simple matter to classify the use of limestone. In fact, such classification has been and is being done regularly and used by United States Bureau of Mines in compiling industry information which is published annually. *Limestone is a bulk commodity which almost exclusively is shipped in carload quantities direct from the point of production to the point of use.* Our invoices and books show definitely the type of user to whom shipments are made. \* \* \* [Italics supplied.]

\* \* \* \*

[335] Mr. LYNCH. Does your proposal contemplate percentage depletion allowance for limestone used in agriculture or roadbuilding or anything of that kind?

Mr. DICKEY. No, sir; it does not. While our com-

pany and our industry makes substantial sales in those fields, it is not necessary to use the grade of limestone required for the chemical and metallurgical use in those uses and we did not feel justified in asking for percentage depletion on that type of stone.

Mr. LYNCH. You are only asking for percentage depletion insofar as limestone is used for metallurgical purposes, is that true?

Mr. DICKEY. That is correct.

Statement of Prof. KENNETH K. LANDES, Chairman, Department of Geology, University of Michigan, Ann Arbor, Mich.

One year ago I prepared for the National Lime Association a survey of domestic high-grade limestone deposits. This survey has been published by that association and distributed to your committee.

[336]

High quality—metallurgical grade—limestone is just as essential to the making of steel as iron ore; it is also necessary for the burning of lime and for the manufacture of many chemicals. Limestone, the rock, is common and abundant in the United States, but metallurgical stone constitutes only a very small part of the total volume of limestone rock. It is a valuable, essential, and exhaustible mineral resource.

[338]

Mr. WOODRUFF. Mr. Chairman, the doctor has a fund of information in this document he has placed before every member of this committee, and I ask

unanimous consent that it may be made a part of the record.

The CHAIRMAN. Without objection, it is so ordered. Thank you very much, Doctor.

Professor LANDES. Thank you.

(The document referred to follows:)

# METALLURGICAL LIMESTONE RESERVES IN THE UNITED STATES

(By Kenneth K. Landes, Ann Arbor, Mich.)

## SUMMARY AND CONCLUSIONS

High-quality (metallurgical grade) limestone is just as essential to the making of steel as iron ore; it is also necessary for the burning of lime and for the manufacture of many chemicals. Limestone, the rock, is common and abundant in the United States, but metallurgical stone constitutes only a very small part of the total volume of limestone rock. It is a valuable, essential, and exhaustible mineral resource.

[339]

KENNETH K. LANDES.

FEBRUARY 5, 1949.

## INTRODUCTION

Limestones, if no limitation as to quality is set, are found very generally in tremendous quantities in most parts of the United States. However, limestones that are of suitable quality and are economically available are a very small proportion of the total of all limestones and are found only in a few areas.

In this report, "limestone" will be used as in industry for both limestone and dolomite, except where

the latter is specifically mentioned. Included within the broad heading "Metallurgical stone" are not only the fluxes used in blast furnace and open-hearth operations but also the purer grades of limestone needed for furnace linings, lime burning, and chemical manufacture. [Italics supplied.]

Limestones that are satisfactory for metallurgical or chemical uses as stone or satisfactory for *raw material* for the production of calcined products may be classified in four grades, as follows: [Italics supplied.]

These specifications are arbitrarily made to provide a means of identifying various classes of limestone, since there are no generally agreed-upon standards. Silica, alumina, and sulfur are impurities. Magnesia is an active basic agent, but limestones with varying proportions of magnesia may have different uses.

By far the greater part of the limestone quarried or mined in the United States has more than the maximum percentage of impurities listed above. This stone is used for concrete aggregate, road metal, railroad ballast, agricultural limestone, cement manufacture, and other purposes where chemical purity is not essential.

#### *Descriptions of uses of metallurgical stone*

Over half of the total volume of stone here classified as "metallurgical" consumed annually is used as blast-furnace flux. The blast furnace is the fundamental unit in the conversion of iron ore to pig iron. \* \* \*



*Metallurgical stone can only be used in lump form.*

The fines produced during mining and processing must be discarded or marketed elsewhere. Furthermore, pulverant types of limestone such as chalk and marl cannot be used for metallurgical purposes, regardless of purity. [Italics supplied.]

\* \* \*

The burning of limestone to produce limes consumes 25 percent of the stone here classified as "metallurgical" each year. One of the most important uses of calcined limestone (lime) is as a flux in the production of steel in the open hearth. Chemical stone, used in making such products as soda ash and calcium carbide, and in the refining of beet sugar, must be of A-1 grade in most instances, although B-1 stone is used in quantity for some purposes. Quality plasters can be made only from A-1 or B-1 stone.

\* \* \*

The total metallurgical stone production is roughly one-third of the annual domestic *crushed limestone* produced (*the amount of limestone mined for building stone is relatively insignificant*). The remaining two-thirds of the *crushed stone* has many uses, especially in concrete and road metal, and as cement stone. For these purposes lower grade stone, which does have large reserves, is adequate; in fact, the more silica and alumina in cement stone the less shale has to be added before burning. The emphasis for stone used in concrete aggregate and road metal is on physical character rather than chemical composition. [Italics supplied.]

\* \* \*

## House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1553] Statement of RALPH L. DICKEY, President, The Kelley Island Lime & Transport Co., Cleveland, Ohio.

Mr. DICKEY. \* \* \*

I am a representative of a committee of the National Lime Association and am requesting that a percentage depletion allowance be provided [1554] for metallurgical and chemical grade limestone at a rate of 15 percent. \* \* \*

Limestone is essential to and used directly in the production of pig iron, steel, caustic soda, soda ash, glass, and sugar, to name only a few important uses.

Lime, which is produced by calcining or burning chemical and metallurgical grade limestone is used by almost every type of industry as well as for the treatment of water, sewage, and trade wastes. Lime is essential in the production of steel, aluminum, magnesium, calcium carbide, and certain explosives from Government ordnance plants. It is also on the atomic energy program, although I do not know how.

[1555] Last year in the report of this committee, you stated, among other things, that, and I quote:

The testimony before your committee revealed that in a number of cases nonmetallic minerals which are not enumerated in existing law are competitive with the minerals receiving percentage depletion or have just as good a claim for such treatment as the enumerated minerals.

In view of the fact that the Congress has recognized the principle of percentage depletion allowances, has

provided such allowances for iron ore and other natural resources certainly no more critical in the economy than high purity limestone, we respectfully request that a percentage depletion allowance be granted to metallurgical and chemical grade limestone at the rate of 15 percent.

(The statement entitled "Metallurgical Limestone Reserves in the United States," by Kenneth K. Landes, referred to, is as follows:)

[This is the same as that submitted during House Hearings in 1950, set forth above at pages 384-386.]

[1566] Statement of PHILIP L. CORSON, G. & W. H. Corson, Inc., Plymouth Meeting, Pa.

Mr. CORSON. My name is Philip L. Corson, and I am president of G. & W. H. Corson, Inc., of Plymouth Meeting, Pa.

The CHAIRMAN. All right, go ahead.

Mr. CORSON. We manufacture lime, refractories, and limestone products from our quarry located near Philadelphia, Pa.

For every ton of steel manufactured, nearly one-half ton of limestone is required—and I repeat that, for every ton of steel manufactured, nearly one-half ton of limestone is required—either in the form of raw limestone, burned limestone, or dead burned dolomitic limestone. \* \* \*

[1568] Mr. JENKINS. Mr. Dickey, I should like to ask you a few questions. How much by way of a de-

pletion allowance did this committee recommend last year?

Mr. DICKEY. 15 percent.

Mr. JENKINS. And we limited that to metallurgical and chemical grades of limestone; did we not?

Mr. DICKEY. That is correct.

Mr. JENKINS. As I remember your statement, I believe you said that common limestone is available and can be found in nearly all parts of the country?

Mr. DICKEY. Ordinary limestone can; that is correct.

Mr. JENKINS. But this type known as metallurgical and chemical limestone is not the ordinary limestone?

Mr. DICKEY. It is far from it. It forms a very small percentage of the total limestone known.

[1569] Mr. JENKINS. I thank you for your answer, for I wanted to bring out the fact that the kind of lime you are talking about is not the common limestone that is present in all parts of the country. I notice that Dr. Landes in his report states that metallurgical- and chemical-grade limestone is produced in four counties in Ohio.

Does the cement industry require this metallurgical and chemical grade of limestone?

Mr. DICKEY. No, sir; it does not. They do not care how much silica or alumina there is in the limestone. Jones & Laughlin Steel Co. bought a large area on the Ohio River, figuring that they would have to go down some 600 or 700 feet to the limestone. But they did not find the operation feasible, and so they sold the property.

Mr. JENKINS. What is the grade of limestone that is used in farming, this limestone that they grind up and use?

Mr. DICKEY. It is the more common type of limestone, and the amount of silica in it doesn't make any difference. They can still use it.

Mr. JENKINS. Is this lime that you are talking about used as fertilizer?

Mr. DICKEY. Only as a byproduct.

Mr. JENKINS. That is because it is too expensive?

Mr. DICKEY. That and the fact that it is too important for other uses.

Mr. JENKINS. Now, in your prepared statement you say that the steel industry depends upon your product in the manufacture of steel?

Mr. DICKEY. Absolutely.

Mr. JENKINS. Can they use the farmer's type of limestone?

Mr. DICKEY. No. It will affect their economy and production, and they can only go so far with it. They really can't use it at all.

Mr. JENKINS. It chokes up their furnaces?

Mr. DICKEY. The purpose of the limestone in the case of pig iron is to remove the silica from the coke, and the more silica you have in the limestone the less effective it is.

Mr. JENKINS. Then limestone is essential in the production of steel?

Mr. DICKEY. Absolutely.

Senate Hearings, 1951

(Senate Hearings, Revenue Act of 1951)

[872] Statement of RALPH L. DICKEY, President, Kelley Island Limc & Transport Co.

[873] I am a representative of a committee of the National Lime Association and am requesting that a percentage depletion allowance be provided for



metallurgical and chemical grade limestone at a rate of 15 percent, as now provided in the bill before you, H.R. 4473. \* \* \*

[874]

(The report submitted by Mr. Dickey is as follows:)

[875] METALLURGICAL LIMESTONE RESERVES IN THE  
UNITED STATES

SUMMARY AND CONCLUSIONS

Limestones that are satisfactory for metallurgical or chemical uses as stone or satisfactory for *raw material* for the production of calcined products may be classified in four grades as follows: [Italics supplied.]

By far the greater part of the limestone quarried or mined in the United States has more than the maximum percentage of impurities listed above. This stone is used for concrete aggregate, road metal, railroad ballast, agricultural limestone, cement manufacture, and other purposes where chemical purity is not essential.

[876]

Metallurgical stone can only be used in lump form. The fines produced during mining and processing must be discarded or marketed elsewhere. Furthermore, pulverent types of limestone such as chalk and marl cannot be used for metallurgical purposes regardless of purity.

The burning of limestone to produce lime consumes 25 percent of the stone here classified as "metallurgical" each year. \* \* \*

The total metallurgical stone production is roughly one-third of the annual domestic *crushed limestone* produced (*the amount of limestone mined for building stone is relatively insignificant*). The remaining two-thirds of the *crushed stone* has many uses, especially in concrete and road metal, and as cement stone. For [877] these purposes lower grade stone, which does have large reserves, is adequate; in fact, the more silica and alumina in cement stone the less shale has to be added before burning. The emphasis for stone used in concrete aggregate and road metal is on physical character rather than chemical composition. [Italics supplied.]

[878] \* \* \* Although a premium grade stone may be sold for low quality uses, an inferior stone cannot be marketed for metallurgical purposes, especially in recent years.

House Hearings, 1953

(House Hearings, General Revenue Revision (1953))

[2091] Statement of E. EIKEL, President, Servtex Materials Co., in Support of Percentage Depletion for Crushed-Stone Producers.

My name is E. Eikel and I am president of Servtex Materials Co., of New Braunfels, Tex. I am also a regional vice president of the National Crushed Stone Association and a member of the board of directors of that association. This statement is presented on behalf of Servtex Materials Co.

First, I want to state that I concur fully in the statement of Mr. Russell Rarey made to the committee on behalf of the National Crushed Stone Association on August 12, 1953.

In addition, I want to identify for the committee some specific problems that Servtex Materials Co. faces under the new percentage depletion regulations of the Treasury Department, as amended.

We produce and market principally *crushed stone* and asphaltic concrete. *Both are produced from limestone of chemical and metallurgical grade*, the latter being a mixture of crushed and screened limestone, water, and liquid asphalt. These materials are in daily competition with rock asphalt and dolomite, both of which enjoy a depletion rate higher than stone. Rates for rock asphalt and dolomite were fixed by Congress without regard to end use. [Italics supplied.]

[2092]

The limestone which we, Servtex Materials Co., New Braunfels, Tex., quarry is of chemical and metallurgical grade. The limestone meets the specifications for chemical and metallurgical grade required by the chemical and metallurgical industries we serve.

\*\*\* This chemical and metallurgical grade limestone also meets the requirements necessary for highway and road construction to which a substantial portion of our quarry output is devoted. *Limestone supplied for highway and road construction and that furnished the chemical and metallurgical industries is all obtained from the identical source or deposit. All of the limestone in the deposit from which we quarry is*

*of chemical and metallurgical grade, regardless of end use. [Italics supplied.]*

#### MAGNESITE

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1953

(House Hearings, General Revenue Revision (1953))  
[2059]

Statement of A. BRENT WILSON, Assistant to President and Director of Northwest Magnesite Corp., Pittsburgh, Pa.

Mr. WILSON. My name is A. Brent Wilson. I am assistant to the president and a director of Northwest Magnesite Corp., Pittsburgh, Pa. This statement is submitted to the Committee on Ways and Means of the House of Representatives, on behalf of my company, which mines magnesite at Chewelah, Wash.

[2060]

#### THE MAGNESITE INDUSTRY

Magnesite is an extremely hard rock, blocky in nature and crystalline in appearance. The deposits occur in lens-shaped bodies, with no continuity between the deposits. Natural magnesite contains small quantities of silica, lime, alumina, and iron oxide as impurities.

The various steps in the mining operations, all performed at the mine, consist of stripping, open-cut

mining, *crushing, concentration, and burning to drive off the carbon dioxide and convert the crude material into a marketable product.* The only product shipped from our Chewelah mine is magnesium oxide in granular form, known commercially as dead-burned magnesite. It is principally used as a raw material for the manufacture of basic refractory brick and to form hearths of furnaces, especially open-hearth steel furnaces. [*Italics supplied.*]

\* \* \* \* \*

MARBLE

(See "LIMESTONE: ALL GRADES . . . PLUS OTHER STONES . . .", INCLUDING . . . MARBLE . . .", *supra*, pp. 363-381.)

OYSTER SHELLS

(See "SHELLS", *infra*, pp. 418-423.)

PERLITE

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[436] Statement of WHARTON CLAY, Secretary-Treasurer, Perlite Institute, New York, N.Y.

\* \* \* \* \*

Mr. CLAY. This is a very young industry; it is not more than 4 years old. \* \* \* Perlite is a volcanic rock which, when heated to a suitable point in its softening range, expands, to make a lightweight aggregate. It is used to improve and lighten the weight of plaster and concrete. It is mined in seven Western States, and is processed in 21 States, including Massachusetts, New York, North Carolina, Michigan, California, and many other States in-between.



In my presentation which has been passed to you, which I request that you put in in full in the record, I have cited several national authorities.

(The statement referred to follows:)

[437]

Statement of Mr. WHARTON CLAY, Secretary-Treasurer of the Perlite Institute.

*Perlite* is the most recently recognized of the lightweight aggregates, and *competes directly in markets throughout the United States with vermiculite*, which presently enjoys the benefits of percentage depletion. [Italics supplied.]

Perlite is a volcanic rock, which when heated quickly to a suitable point in its softening range, expands to form a lightweight, noncombustible, glass-like material of cellular structure.

*It is used* to improve and lighten the weight of plaster and concrete. Improvements consist in the greater insulation value of the product and greater fire protection. Perlite competes in these characteristics directly with vermiculite and has achieved the same recognition in building codes as a fire protection medium that vermiculite has enjoyed for a number of years. [Italics supplied.]

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1650] Statement submitted by Mr. WHARTON CLAY, Secretary-Treasurer of Perlite Institute.

I wish to avoid a repetition of the detailed instances of such competition which have previously

been presented to the Ways and Means Committee in the hearings in connection with the 1949 and 1950 Revenue Revisions. I list below the additional *adaptations of perlite* which have come to my attention since my last testimony before the Ways and Means Committee. [Italics supplied.]

\* \* \* \* \*

**PHOSPHATE ROCK**

(Percentage depletion first allowed beginning with 1947)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[380] Statement of KENNETH B. RAY, Counsel for Food Machinery & Chemical Corp., and also Representing Phosphate Rock Industry Group.

\* \* \* \* \*

[382] In 1947 the benefits of percentage depletion were also extended to phosphate deposits. This turned out to be a particularly wise piece of legislation since the Government for many years had been endeavoring to secure widespread development of the phosphate deposits of southeastern Idaho. Following the addition of phosphates to the statute this company has expended over \$10,000,000 in an electric furnace project to utilize the Idaho phosphate deposits. The economics of this development are based on *percentage depletion for the basic raw material, phosphate rock*. \* \* \* [Italics supplied.]

\* \* \* \* \*

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1637] Statement of KENNETH B. RAY, New York, N.Y., Counsel for Food Machinery and Chemical Corp., New York, N.Y.

Mr. RAY. Mr. Chairman, and gentlemen of the committee, my name is Kenneth B. Ray. I am appearing on behalf of a large segment of the phosphate rock industry, many of whose representatives are here today. I am also counsel for Food Machinery & Chemical Corp. which is engaged not only in the development of phosphate deposits in the West but is also mining trona in southwestern Wyoming.

\* \* \* \*

[1638] NONMETALLIC MINERALS ESSENTIAL TO AGRICULTURAL PRODUCTION

Ninety percent of the 9 to 10 million tons of *phosphate rock* mined annually in the United States is *for use by farmers*. A reduction in the percentage depletion rate would almost certainly result in an increased selling price of *fertilizer sold to farmers*. The same statement applies to potash, about which I understand its representatives will testify. \* \* \* [*Italics supplied.*]

\* \* \* \*

Senate Hearings, 1954

(Senate Hearings, Internal Revenue Code of 1954)  
[1334]

\* \* \* \*

Statement of JAMES M. GILLET, Victor Chemical Works, Chicago, Ill.

Mr. GILLET. My name is James M. Gillet. I am assistant to the president of Victor Chemical Works, Chicago, Ill.

Victor Chemical Works, Mr. Chairman, is a chemical manufacturing firm that has plants in Montana, California, Illinois, Tennessee, Florida, and Pennsylvania. Most of our operations are connected with the *production of phosphates, starting with phosphate rock and continuing through to the production of*

*some 150 chemicals* that are used in practically every industry in the country. [Italics supplied.]

I appear before you in connection with a request to clarify section 613 of the code. \* \* \*

[1335]

(The statement referred to follows:)

#### BRIEF OF VICTOR CHEMICAL WORKS

It is respectfully requested that section 613(c)(4)(E) of the proposed Internal Revenue Code of 1954 be amended as follows: Subsection (4)(E), after the words "burning of magnesite", add the words "and the *sintering* and *nodulizing* of phosphate rock". [Italics supplied.]

*The sole purpose of the amendment is to clarify the meaning of the term "ordinary treatment process" as applied to phosphate rock in determining percentage depletion, so that the miner of phosphate rock may have a definite basis for determining his proper tax.* [Italics supplied.]

[1337]

Mr. GILLET. \* \* \*

The matter that I am referring to principally is the sintering of phosphate rock. \* \* \* In order to use this rock in the production of phosphorus it is necessary that it be in lump form. The powdered, low-grade phosphate rocks, unless they are made into lump form, will not function in the furnace. [Italics supplied.]

Originally most of the phosphorus was produced from high-grade rock which was mined as pebbles or as plate in Tennessee, but since the growth of the

phosphate industry the supply of the lump rock is not enough for the industry.

It has been necessary for us to go to the use of low-grade rocks, which, incidentally, have no other use at all, except in the production of phosphorus and to treat *(those rocks by sintering, in order to make big particles out of little ones. [Italics supplied.]*

The income-tax returns are being filed now on the basis that sintering is an ordinary treatment process. \* \* \*

The CHAIRMAN. Is it a common practice to sinter that rock, by other companies?

Mr. GILLET. It is, yes sir.

The CHAIRMAN. It is a general commercial practice?

Mr. GILLET. Those who make phosphorus, yes sir.

We would request, then, that subsection E—that is the last item in section 613—be amended by addition of the words “by the sintering and nodulizing of phosphate rock.”

Some people say they are sintered and others say nodulized, but it is the same thing.

The CHAIRMAN. What is the sintering process?

Mr. GILLET. As we apply it, it consists of putting the powdered rock into a kiln, a rotary kiln where it is heated by a gas flame from natural gas, or by-product gas, or powdered coal. As it passes down through the kiln it warms up and gradually gets sticky. When it reaches the bottom of the kiln it is hot enough for these small particles to stick together. Those are discharged onto a moving grate where they are treated with a blast of air to cool them and they are then ready to put on the stockpile for use as a raw material in the production of phosphorus. There



is no chemical change involved and it is merely a physical operation.

# POTASH

(Percentage depletion first allowed beginning with 1944)

Senate Hearings, 1943

(Senate Hearings, Revenue Act of 1943)

[363] Statement of F. O. DAVIS, Treasurer, Potash Co. of America.

[366] (The memorandum submitted is as follows:)

## MEMORANDUM RE PERCENTAGE DEPLETION FOR POTASH

[369] IV. Income "from the property."

In the case of the leading brine producer, the mineral property consists of a nonreplenishing subterranean lake of heavy brine containing the potash in solution. The brine is pumped from the lake by means of drilled wells, and the potash is extracted from the brine at the lake site by means of unique *evaporation and crystallization processes* developed by the company for that purpose. The brine recovered from the company's potash deposits also contains varying amounts of borax, soda ash, and salt cake, and small quantities of lithium phosphate and bromine. \* \* \* [Italics supplied.]

The *evaporation and crystallization processes* are elaborate in nature. Brine is pumped continuously through a series of processes which constantly require

delicate adjustments of temperature, pressure, etc., and chemical analyses of the liquors and products. The separation of the chemical constituents hinges on their differing limits of solubility at different temperatures and under varying pressures.

A characteristic feature is the evaporation of the liquor at high temperatures (except for which the liquor would be supersaturated) followed by quick cooling to a point at which a particular salt will be precipitated in solid form, while other constituents remain in solution. At one stage of the general process, soda ash, and salt cake are partially segregated, and at another stage, but while the liquor still contains about half the potash, borax is removed. Having gone through the process, the liquor is then repeatedly turned back along with the incoming fresh brine from the lake deposit and goes through the whole cycle again and again for further removal of the potash and other products.

[370] Respectfully submitted.

AMERICAN POTASH & CHEMICAL CORPORATION  
INTERNATIONAL MINERALS & CHEMICAL CORPORATION  
POTASH CO. OF AMERICA  
UNITED STATES POTASH CO.

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[383] Statement of FRED O. DAVIS, Vice President and Treasurer, Potash Co. of America, Carlsbad, N. Mex.

[386] Mr. LYNCH. Mr. Davis, is it not so that the United States Court of Tax Appeals found as a fact that the discovery value of potash was 85 cents?

Mr. DAVIS. Eighty-five cents per ton was the figure granted under the discovery depletion case of United States Potash Co.

Mr. LYNCH. Did not the Bureau afterward set it on the basis of 82½ cents per ton?

Mr. DAVIS. I believe 85 cents was the final figure.

Mr. LYNCH. Eighty-five.

Mr. DAVIS. Yes, sir.

Mr. LYNCH. What is the price of potash f.o.b. mines?

Mr. DAVIS. The crude product is worth about \$4.50 per ton of ore. The refined product, which takes 2½ tons to produce, is about \$20 per ton.

Mr. LYNCH. Does not the figure go up as high as thirty or thirty-five dollars per ton?

Mr. DAVIS. No. The highest grade of potassium, which is sold from Carlsbad, which is muriate of potash of 61- or 62-percent grade, sells for approximately \$20 per ton.

Mr. LYNCH. Is that the very highest?

Mr. DAVIS. There is a commercial chemical grade of potash which gets a premium of a few dollars, about \$2 a ton.

Mr. LYNCH. The Government figures that we had indicated that it was about \$35 per ton.

Mr. DAVIS. They are undoubtedly speaking about the K<sub>2</sub>O content of the product. Muriate of potash of a pure grade is 63 percent, and that is the product that sells in the neighborhood of \$21 a ton. The potassium content of that is worth about \$34 a ton. But that is not the product on which an 85-cent per ton discovery allowance was granted. It was crude ore.

Mr. LYNCH. It is the same potash, is it not? It is from the same mine; is it not?

Mr. DAVIS. But it is a different grade.

Mr. LYNCH. It may be of a different grade, but the discovery value of potash, 85 cents, is a matter of court record, is it not?

Mr. DAVIS. That is correct. There was a discovery value of 85 cents per ton granted.

[387] Mr. DAVIS. Possibly your figure of \$34 a ton is the delivered price to eastern seaboard. That may be where you get your figure. *Of course your percentage depletion does not go on the delivery price. It is f.o.b. basis. [Italics supplied.]*

Mr. LYNCH. *It is f.o.b. mines. [Italics supplied.]*

Mr. DAVIS. *Yes; and that figure is \$20 a ton. [Italics supplied.]*

CARLSBAD, N. MEX., February 20, 1950.

[2231] Hon. WALTER A. LYNCH,  
Ways and Means Committee,  
House of Representatives, Washington, D.C.

DEAR SIR: This is to clarify the colloquy we had in the course of my testimony before the Ways and Means Committee on February 9, 1950, in support of the present rate of percentage depletion for potash.

The depletion of 85 cents per ton based on discovery value fixed by the Board of Tax Appeals in United States Potash Company, Inc. (memorandum decision, August 16, 1941; CCH Dec. 12,046-A) was based on crude ore. Percentage depletion, however, under section 114(b)(4)(B) of the Internal Revenue Code is allowed with respect to refined ore. Said section defines the "gross income from the property" as the gross income from mining and prescribes that "mining" shall be deemed to include ordinary treatment processes normally applied by mine operators to ob-

tain a commercially marketable product. Under subdivision (iv) of said section such "ordinary treatment processes" with respect to potash include crushing, grinding, beneficiation by concentration, etc.

The price for refined potash is, as I testified, \$20.13 f.o.b. Carlsbad, N. Mex. From this must be deducted the royalty averaging 50 cents per ton of refined product payable to the Government of the United States or the State of New Mexico, so that the figure to which the 15 percent depletion rate is applied is \$19.63, resulting in a deduction of about \$2.94 per ton of refined ore (\$19.63 plus 15 percent).

It takes between 2.75 and 2.85 tons of crude ore to obtain one ton of the average highest grade potash commercially produced which contains about 61 percent K<sub>2</sub>O and sells for about 20 per ton. Hence, the true comparison is not between a deduction of 85 cents discovery depletion and \$2.94 percentage depletion, but between 85 cents multiplied by from 2.75 to 2.85, or from \$2.32 to \$2.42 and \$2.94.

Finally, I should like to reiterate that no percentage depletion is being taken on potash selling at \$35 per ton. Thirty-five dollars would be the theoretical price at which pure potash (100 percent K<sub>2</sub>O) should sell, but no such mineral is commercially produced. Occasionally, potash running as high as 63 percent K<sub>2</sub>O is sold, but 61 percent K<sub>2</sub>O is the average highest grade potash which is commercially produced.

I should appreciate it if you would cause this letter to be printed in the record of the hearings in conjunction with my oral testimony.

Respectfully,

F. O. DAVIS,  
Vice President and Treasurer,  
Potash Co. of America.



(House Hearings, Revenue Revision of 1951)

[1621] Statement of Fred O. Davis, Vice President and Treasurer, Potash Co. of America, Carlsbad, N. Mex.

Mr. DAVIS. My name is Fred O. Davis, vice president and treasurer of the Potash Co. of America located at Carlsbad, N. Mex. This statement is submitted in behalf of the Potash Co. of America and other producers of potash in the United States.

The inclusion of potash in the percentage depletion of our revenue acts has been relatively recent, having been included for the first time in 1943. \* \* \* At the time potash was first included for percentage depletion it was recognized that the mineral was unique in its needs because of several features:

4. Potash is mined in only one small area of the United States, near Carlsbad, N. Mex., where nearly 90 percent of the production is secured. Practically all of the remainder comes from brine deposits in California and Utah.

[1626] Mr. JENKINS. I have one question, Mr. Davis. What does potash consist of or look like in the mines?

Mr. DAVIS. It is a soluble salt. It is usually found with sodium chloride. Potash itself is potassium chloride and it is found with sodium chloride, and *the process consists of separating the potassium from the sodium.* In our case it is raw salt embedded 1,000 feet underground. [Italics supplied.]

Mr. JENKINS. What is its color?

Mr. DAVIS. It is white. It looks very much like table salt.

## QUARTZITE

(See "CLAY REFRACTORY AND FIRE",  
*supra*, pp. 335-342.)

## ROCK ASPHALT

(Percentage depletion first allowed beginning  
with 1942)

Senate Hearings, 1942

(Senate Hearings, Revenue Act of 1942)

[1405] Senator THOMAS. \* \* \*

[1406] The amendment which I submit for the record—and I will ask to be made a part of the record at this point—adds rock asphalt along with metals.

Senator VANDENBERG. What is rock asphalt?

Senator THOMAS. Rock asphalt is a sort of sandy substance originally that was impregnated with oil, but because of the location of the oil pool the oil has drained away, leaving a sand containing more or less of the oil on the sand, which makes it a substance that can be taken from the mine. Sometimes it is a rather solid substance like the crust of a concrete sidewalk, but it is a sand containing oil that can be ground, and it contains enough oil that, when it is *ground* and then put together again and rolled it makes a solid substance again. [Italics supplied.]

Now, that is one form of the rock asphalt.

The second form is found in pools of sand. The sand is more or less black and sometimes you can pick it up on your hand and squeeze it, and you could almost see your oil in the sand.

That sort of asphalt is mixed with more limestone and more sand to make it of a certain consistency.

Then when it is at the proper consistency it is placed on the road or on the street or on the airport landing areas, and rolled cold and immediately it is susceptible of being traveled over, and it is used for the building of roads and for the building of streets and for making, now, runways for airports.

\* \* \* \* \*

[1409] Statement of GEORGE E. H. GOODNER, Washington, D.C., representing rock asphalt producers.

\* \* \* \* \*

[1410] Rock asphalt, as the Senator has told you, is a material composed of rock—either limestone or sandstone—and the residuum from petroleum or asphaltum.

It was formed by nature thousands of years ago, by the oil impregnating the porous layers of rock or stone. Then, through some geologic process, the oil was drained off or forced off, leaving the residuum which is asphalt, and when a particle or a piece of this rock asphalt is crushed to the minutest particles, every particle is impregnated with asphalt.

Therefore, it makes a very highly desirable road or airport runway material.

*It is mined with steam shovels after being blasted out of position. It is crushed to required size, laid on the road, and rolled cold, and as soon as it is rolled the road is ready for use. [Italics supplied.]*

It is waterproof; it is solid; it resists wear

\* \* \* \* \*

[1411] Senator BARKLEY. We have a number of asphalt deposits in my State which we regard very highly. It is recommended by road builders, and many of our roads have been built with rock asphalt.

*As you say, it requires no treatment at all, except the matter of pulverization. [Italics supplied.]*

\* \* \* \* \*

Mr. GOODNER. It stands in a group by itself, because it is a road preparation made by nature, but it is very closely allied to the oil industry, because the residuum from the oil is what, mixed with the rock, makes the product.

Senator BARKLEY. It is natural asphalt, whereas the kind you have to mix with oil is an artificial asphalt?

Mr. GOODNER. It is prepared, and it comes directly in competition with those, although they have enjoyed the 27½ percent depletion allowed to the oil industry, and the rock asphalt enjoys no such allowance.

[1412] Mr. GOODNER. \* \* \*

Now, this is a small industry—the rock asphalt industry—compared with the ones you have been hearing about today.

Senator CONNALLY. Let me ask you there: Isn't it also true that the rock that it is in has to be a peculiar formation, that every sand wouldn't create rock asphalt?

Mr. GOODNER. That is true.

Senator CONNALLY. And the difference between rock asphalt and other asphalt is that this is in a sand or in a rock. It is porous. Nature just combined the oil and the rock to make a prepared product itself, whereas in the other asphalts it is the residuum or the base of heavy oils, and that is the stuff you see out on the highway, where they heat it, boil it, and then pour it on the rock surface, whereas the rock asphalt is not treated like that but it is laid cold, isn't it?

Mr. GOODNER. That is absolutely correct, Senator.

[Brief for rock asphalt industry appears at pages 1413-1417.]

Senate Debate, 1942

[(88 Cong. Record (Part 6), 77th Cong., 2d Sess.)]

[8022] Mr. THOMAS of Oklahoma.

[8023] Mr. President, let me say just a word about rock asphalt. Rock asphalt is found, I think, in a number of States. Rock asphalt is a residue of oil. Some time way back in ancient times oil in places was near the surface of the ground. This oil was imbedded in sand. In some way the oil seeped away from the sand but left the sand covered with oil. If we take out this sand which is thoroughly covered with oil and spread it out on the road and roll it cold on the road, in a few minutes' time the road can be traveled in safety and with no injury to such road. That is rock asphalt. It is a product which is used for road building, a product which is used for street building, and a product which is now being used to make the hard-surface runways on thousands of miles of airports throughout the United States. \* \* \*

As I said, the companies which are producing asphalt are small. They operate only in the local community. They get the asphalt as previously stated, from near the top of the ground. *Production is largely a matter of labor.* Not much machinery is required to develop and operate an asphalt mine. The top of the ground is stripped off, and then the rock-asphalt sand is taken out. Then this oil-impregnated and oil-covered sand is spread on the road cold, lev-



eled, and rolled down, and the moment it is rolled the road is ready to travel. [Italics supplied.]

House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

[57] Statement of D. L. STREET, Louisville, Ky., representing Rock Asphalt Industry.

THE ROCK ASPHALT INDUSTRY AND PERCENTAGE DEPLETION—A STATEMENT OF THE NEED FOR CONTINUATION OF PERCENTAGE DEPLETION OF ROCK ASPHALT DEPOSITS.

The following information has been compiled in support of the contention of the rock asphalt industry that percentage depletion should be continued for the industry on a permanent basis.

#### GEOLOGY AND RESERVES

Rock asphalt was formed thousands of years ago by the infiltration in limestone and sandstone of petroleum having an asphalt base. Thereafter, geologic changes caused the lighter oils of the petroleum to run off or to evaporate, leaving the stone impregnated with asphalt amounting generally to from 5 to 15 percent of the combination.

#### PRODUCTION AND TRANSPORTATION

The rock asphalt industry as a whole is still in its infancy, although several concerns are producing in excess of 100,000 tons a year.

[58] The production of this resource in the United States during the 10-year period ending in 1940 was as follows:

Production figures for the years following 1940 are not immediately available.

Imports and exports of rock asphalt are negligible. In view of the weight of the product a certain limitation on the market is created by freight charges, but, due to the wide distribution of the deposits, shipment to most of the States is practicable. In fact, Kentucky has shipped rock asphalt to 33 States.

#### USES

Since "nature made the mixture," *rock asphalt can be used with a minimum of effort*, primarily because it can be laid "cold." [Italics supplied.]

Probably 90 percent of all rock asphalt being produced in the United States is used for paving surfaces such as highways, airport runways, and factory floors. It is also used on tennis courts and playgrounds.

[60] Respectfully submitted.

D. L. STREET,  
Louisville, Ky.

Appearing for:

ALABAMA ASPHALTIC LIMESTONE Co.,  
Birmingham, Ala.

KENTUCKY ROCK ASPHALT Co.,  
Brownsville, Ky.

SOUTHERN ROCK ASPHALT Co.,  
Oklahoma City, Okla.

UVALDE ROCK ASPHALT Co.,  
San Antonio, Tex.

WHITE'S UVALDE MINES.,  
San Antonio, Tex.

CALROCK ASPHALT Co.,  
San Francisco, Calif.

**Mr. STREET.** Rock asphalt was formed thousands of years ago by the infiltration of petroleum with asphalt base, in either sandstone or limestone.

Later on, through geological changes, the oil seeped off or dried up, leaving the stone impregnated with this asphalt, which of course made an asphalt stone.

[61] The deposits are found primarily in Kentucky, Alabama, Texas, Oklahoma, and California, with some deposits in New Mexico, Missouri, Utah, and Colorado.

The material is shipped widely in a number of States although freight charges restrict its distribution.

*The material is used almost exclusively for paving purposes.* It is unexcelled in one respect for paving purposes: Where a highway has worn out, and it is not necessary to replace that highway entirely, a three-quarter inch or inch spread of natural rock asphalt over the highway will restore the highway without touching the base, unless the base happens to be broken. [Italics supplied.]

This material, being a *natural material*, is equal to or superior to many of the mixes that are used on highways, tennis courts, and in other places where you need a paving material. [Italics supplied.]

\* \* \* \* \*

#### SAND AND GRAVEL

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[310]

\* \* \* \* \*

Statement of J. RUTLEDGE HILL, Chairman, National Sand and Gravel Association, Dallas, Tex.

[315] Mr. MILLS. Mr. Hill, what is the price of sand and gravel which you would use for purposes of percentage depletion?

Mr. HILL. That, as I understand it, sir, would be the selling price less transportation costs.

Mr. MILLS. About 90 cents?

Mr. HILL. The average in the table shows 91 cents, sir.

Mr. MILLS. Then percentage depletion at 15 percent on a 90-cent price would be equivalent to about 13½ cents per ton, would it not?

Senate Hearings, 1950

(Senate Hearings, Revenue Revisions of 1950)

[793] Statement of J. RUTLEDGE HILL, Dallas, Tex., appearing as Chairman, Committee on Taxation, National Sand and Gravel Association.

[794] Mr. HILL. If we find that there is sufficient sand and gravel to justify the acquisition and the possible marketing of it, we acquire the property, and we erect a processing plant, which consists of *crushing, washing, sizing, screening, grading, and recombining*, to form the particular material that the architect or the engineer may specify for a given job. There are certain sizes, small to large, and they must be uniformly graded from small to large; and then the sand must be clean, sharp, well graded, from the 200 mesh sieve, which, by the way, is so small that water won't go through it, up to a quarter inch. [Italics supplied.]

When all that preparation has been made, it is then loaded on to a vehicle for delivery to the user.

The CHAIRMAN. Is your plant generally connected with the gravel pits or the place where you mine it? Do you have to transport it any distance?

Mr. HILL. A relatively short distance, sir. The plant is always relatively close to the point of processing.

The CHAIRMAN. In the case of sand and gravel, you say that is true always?

Mr. HILL. In the case of sand and gravel; yes.

The CHAIRMAN. But there is some transportation cost there, is there?

Mr. HILL. In getting the raw material from the point of extraction to the processing plant.

The CHAIRMAN. *It is necessary to get it to this processing plant and take this step in processing it in order to make it marketable?* [Italics supplied.]

Mr. HILL. That is correct, sir.

Senate Hearings, 1951

(Senate Hearings, Revenue Act of 1951)

[885] Statement of J. RUTLEDGE HILL, Chairman, Committee on Taxation, National Sand and Gravel Association.

In behalf of the commercial sand and gravel industry of the United States, I respectfully request your committee to recommend to the Senate that it concur in the action of the House of Representatives which would add sand and gravel to the list of non-metallic minerals entitled to percentage depletion.

[889] *Sand, to be usable, has to be graded from very fine particles which will pass the screen that water will not even go through, on up to the larger particles,*



and there must be a smooth gradation from the small up to the large, and for that reason 98 percent of the sand found in nature is useless to these industries. [Italics supplied.]

Do I make myself clear?

The CHAIRMAN. Yes, I think I understand you.

Is there any chemical process by which you could take ordinary sand and convert it into usable form?

Mr. HILL. No, Senator. Most of the sand that you have in mind is extremely fine.

The CHAIRMAN. Yes.

Mr. HILL. And the problem is to incorporate and build up a material that goes from fine up to about a quarter inch in size.

\* \* \* \* \*

House Hearings, 1953

(House Hearings, General Revenue Revision)

[2087] Statement of J. RUTLEDGE HILL, Dallas, Tex., Chairman of Committee on Taxation, National Sand and Gravel Association, in re Topic 38, Depletion and Exploration Expenditures.

\* \* \*

[2089]. \* \* \* *Industrial sand is a raw material* used principally in the foundry, glass, and chemical industries, but also finding employment for many other purposes. \* \* \* [Italics supplied.]

\* \* \*

SHALE

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1953

(House Hearings, General Revenue Revision (1953))

[2099] Statement of NATIONAL CLAY PIPE MANUFACTURERS, INC., Washington 6, D.C.

This statement is presented on behalf of the vitrified clay sewer pipe manufacturers of the United States for the purpose of (1) urging that fire clays and shales be continued on the eligibility list of minerals entitled to percentage depletion, and (2) ask that consideration be given to a more equitable depletion rate for refractory type shales.

Vitrified clay sewer pipe is *manufactured* and sold under rigid specifications by the American Society for Testing Materials. \* \* \* [Italics supplied.]

The *minerals used* by this industry are found in limited quantities \* \* \* [Italics supplied.]

Generally speaking, two types of *materials* are required in the *manufacture* of pipe, i.e., refractory or fire clay and high grade or refractory type shales. The refractory clay helps maintain the shape and dimensions of the product during the burning process and the refractory type shale adds strength and minimum absorption. [Italics supplied.]

The present law provides percentage depletion rates for clays and shales *used* in the *manufacture* of sewer pipe as follows: [Italics supplied.]

	Percent
Shale .....	5
Refractory and fire clay .....	15

The type of shales *usable* in the production of sewer pipe are at least as scarce and as difficult to locate as fire clays, for which a 15-percent depletion rate is provided. Usable refractory type shale is like oil, "it's where you find it" and for that reason such shale should be entitled to the same 15-percent rate that is allowed for refractory and fire clay. \* \* \* [Italics supplied.]

## SHELLS: CLAM AND OYSTER

(Percentage depletion first allowed beginning with 1951)

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[471] Statement of W. P. HAMBLÉN, Houston, Tex.

Mr. HAMBLÉN. Mr. Chairman and gentlemen of the committee, I am W. P. Hamblén, of Houston, Tex. I am appearing on behalf of a number of companies engaged in the production of mineral shell deposits. I am a director and an attorney for the W. D. Haden Co., of Houston, Tex., one of the larger producers of mineral shell in the State of Texas.

The principal *production of mineral shell for commercial use* occurs in the Gulf coast area. This production is obtained by a complicated dredging process from prehistoric deposits in the form of reefs. These deposits are nonmetallic mineral deposits and have been determined so to be by the Federal courts. [*Italics supplied.*]

[472] The shell industry as we know it began on a very small scale about 40 years ago in and near Galveston, Tex., and has since developed throughout the Gulf coast area. The growth and importance of the shell industry today is readily illustrated by pointing out its history in the south Texas area. At first it was only used as a surfacing material for streets and roads. Then the railroads began to use it as a ballast material. In 1916, at Houston, the Lone Star Cement Co. opened the world's first cement plant, using this shell as a raw material, and about 10 years later, the Trinity Portland Cement Co. opened a sec-

ond plant in Houston, using mineral shell as a material and as a base in the manufacture of cement.

In 1929 the W. D. Haden Co. opened a plant near Houston, which produced lime from mineral shell. Subsequently, Mathieson and Southern Alkali Corp. opened their Texas plants using mineral shell to make lime. The lime, in turn, is used to make caustic soda and soda ash. Caustic soda, as most of you doubtless know, is used in making soap, rayon, lye, in vegetable-oil refining, in paper making, in oil refining, in wool scouring, and in the manufacture of glass. The availability of caustic soda made from lime produced from shell, caused construction of many plants in Texas for almost all of these processes. One of the plants using caustic soda made from shell is Celanese, established at Bishop, Tex., about 1942. This plant uses mineral-shell caustic soda to make chemicals essential in the manufacture of fabrics; plastics, textiles, drugs, varnishes, lacquers, dyes, papers, fungicides, antifreeze, soaps and antirust material, and many other products, including film for the making of moving pictures.

In 1936 the Champion Paper Co. built its plant in Houston and became a large user of shell transforming it into lime, and in 1940 Dow Magnesium Co. established its plant at Freeport and became one of the world's largest consumers of shell. It makes shell into lime and uses the lime to precipitate magnesium from sea water. The fact that shell is almost a pure calcium carbonate (I understand that it runs from 98½ to 99½ percent pure calcium carbonate), makes it particularly adaptable for the uses I have mentioned.

The Ideal Cement Co. has constructed a cement plant at Houston, using mineral shell as one of its raw materials and the Halliburton cement plant, now under construction at Corpus Christi, is absolutely

dependent upon shell. Today, only about one-fourth of the Texas shell production is used for road surfacing:

[473]

\* \* \* During the war years, *enormous amounts of shell were being used* in construction of airfields, roads to war plants and docks, and the cement plants increased their demand for shell on account of the great demand for cement and Dow Magnesium was making increasing demands due to its strategic position in the war effort. [Italics supplied.]

The equipment for the proper and economic production of shell consists of dredges, tugboats and especially constructed barges, as well as docks and unloading facilities. \* \* \*

Mr. SIMPSON. Are these shells lime, calcium?

Mr. HAMBLIN. They are prehistoric deposits.

Mr. SIMPSON. Chemically what are they?

Mr. HAMBLIN. They make lime largely, used in making cement. They crush them to make cement, mix them with clay.

Senate Hearings, 1950

(Senate Hearings, Revenue Revisions of 1950)

[703]

Statement of W. P. HAMBLIN, Director and Attorney for the W. D. Haden Co., accompanied by W. Parker, President, Parker Bros.

[704] Mr. HAMBLIN. My name is W. P. Hamblin, of Houston, Tex. I am one of the directors and attorney



for the W. D. Haden Co., one of the largest producers of oyster shell.

I have with me Capt. W. Parker, who is president of Parker Bros., who is a producer of oyster shells in the Texas area.

There has been a great deal of confusion about what we mean when we speak of the oyster shell industry. Most people think that we use the shucked shell, or that we are gathering shells from the sea which are continually being replaced. That is not true.

The Government has said that it is a mining operation. It is a fossil shell that has been deposited hundreds of million years ago—we do not know how many. We reach that with a dredging process, going down underneath the bottom of the bays 2 to 4 feet, moving that much silt, and then reaching this fossil shell.

Senator CONNALLY. In other words, the shell is covered up with silt?

Mr. HAMBLIN. The shell is covered up with silt, anywhere from 2 to 4 feet.

Senator CONNALLY. You have to dredge that off?

Mr. HAMBLIN. We have to dredge that off and then *get the shell, take it up to the top of our dredges and wash it and screen it*; and the fines, the smaller shells, go into one barge and the heavier shells go into another, because the cement plants and the chicken-feed plant and the fertilizer plants want the finer shell. The other shell can be used for other purposes. The Dow Chemical Co., for instance, uses a vast quantity of our shell and does not require the fine. I think their monthly requirement is 54,000 yards of shell. Each one of the cement plants in Houston requires approximately a thousand yards a day. The chicken-feed plant will probably require a thousand yards three times a week and so on. [Italics supplied.]

(Senate Hearings, Revenue Act of 1951)

[858] Statement of W. P. HAMBLEN, Houston, Tex., representing various gulf coast mineral shell producers.

Mr. HAMBLEN. My name is W. P. Hamblen, of Houston, Tex., representing a number of gulf coast shell industries, producing mineral shell.

Mr. Chairman and gentlemen, I have filed a statement with the committee which I would like to ask to be considered as part of the record.

The CHAIRMAN. Yes, sir.

[859]

(The statement of Mr. Hamblen is as follows:)

Statement of W. P. HAMBLEN, of Houston, Tex., representing various gulf coast mineral shell producers.

Shell is produced by means of large dredges that bring the shell up from the bottom of the bay, carry it up to the top of the dredge where it goes down chutes [860] and is *washed* continuously and finally delivered into barges. There is a *method on board the dredges of separating the fine shells from the large*. The fine shell is used mostly by the chicken feed industry and the cement plants, although the cement plants have to take some of the larger shell as we are unable to produce enough of the fines from them to operate continuously. The other companies, such as Dow Chemical, Mathieson Chemical Co., and the alkali companies use the larger shell as it is more

adaptable to their use from a processing standpoint.  
[Italics supplied.]

SLATE

(Percentage depletion first allowed beginning  
with 1951)

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1646] (The following statements were submitted  
for the record:)

Statement of WINSTON L. PROUTY, M. C., Vermont,  
regarding the need for percentage depletion for the  
slate industry.

I would like to submit for the consideration of  
the committee a few reasons why I believe the slate  
industry should be given the benefit of percentage  
depletion.

As is quite commonly known the slate industry is  
made up primarily of small businesses. According  
to the Bureau of Mines there were 80 operators in  
1949 doing a business of \$12,200,000. This means  
about \$150,000 apiece. The industry is located prin-  
cipally in Pennsylvania, Vermont, and New York  
State with scattered quarries in Arkansas, California,  
Maine, Georgia, Maryland, and Virginia. Recent  
years have seen the slate industry considerably weak-  
ened by the following features.

[1647] It seems only equitable that the slate industry  
should be given the same consideration as is given  
its competitors.

(Senate Hearings, Revenue Act of 1951)

[834]

\* \* \* \* \*

Statement of W. F. BRONKIE, West Pawlet, Vt.

Mr. BRONKIE. My name is W. F. Bronkie, representing the slate industry of the country, particularly the Vermont-New York Slate Association, the Pennsylvania Slate Association, and the slate producers of Maine and Virginia.

Senator HOEY. You may proceed, Mr. Bronkie.

Mr. BRONKIE. We have a very simple request to ask. The slate industry is a very small business. You have in past tax laws recog-[835]nized the percentage depletion factor as important to the mining and quarrying industry.

During all these years, slate has been overlooked.

It has been put into the House bill, but it has been tied to a low-cost bulk product, stone, whereas slate is a specialized product, higher in value and quality, and should be given a separate identity, the same as any other competitive or comparative nonmetallic mineral product.

Senator MILLIKIN. What is its state in the earth, as distinguished from granite or marble? Does it present the same appearances? Does it present the same mining problem?

Mr. BRONKIE. Exactly; the same mining problems as talc, feldspar, and other minerals that are already getting the percentage depletion in their own right.

\* \* \* \* \*

Senator MILLIKIN. Where are your slate quarries located?

Mr. BRONKIE. In a very limited area in Vermont and New York. They run about 25 miles long and 2 or 3 miles wide.

Senator MILLIKIN. They do not occur generally over the United States?

Mr. BRONKIE. There is that one area in Vermont, as I mentioned. Another is in Virginia, around Buckingham and Arvonnia.

Senator MILLIKIN. And does commercial production come only from those areas that you have mentioned?

Mr. BRONKIE. Yes, sir.

Senator MILLIKIN. *What are the relative costs of producing the slate, as distinguished from reducing other quarry material to commercial form? What do you do with a block of slate at the quarry? [Italics supplied.]*

Mr. BRONKIE. We first have to quarry it, and get it out of the ground in a whole piece. It is the reverse of an ore mining operation that we try to keep our pieces as large as we can.

Senator MILLIKIN. Yes.

Mr. BRONKIE. And it is brought out and cut up either on a diamond saw or by cold cutting methods. It is put into a working group where it is split and trimmed and given its shape. There are further processes in surfacing, sandrubbing, fitting to setting diagrams for laying on the floor, or drilled for electrical switchboards.

[836] Senator MILLIKIN. You have outlined quite a comprehensive and expensive process.

Senator TAFT. How does it come? In slices?

Mr. BRONKIE. In beds.

Senator TAFT. Yes. But is there something in between? Do you have a layer of slate and then a layer of something else and then a layer of slate?

Mr. BRONKIE. We have impurities in it from place to place.

Senator TAFT. How do you get a piece of slate, or a shingle?



**Mr. BRONKIE.** *You get a large block out, and a man sits there with a hammer and a chisel and splits it. [Italics supplied.]*

**Senator TAFT.** He slices it to make it thin?

**Mr. BRONKIE.** He slices it. It has a natural cleavage in a natural slice. It is peculiar to slate. That is why not all slate has it. We think we have a quarry, but it does not have a good cleavage; so it is not a commercial slate quarry.

**Senator MILLIKIN.** What would you like to see in this law?

**Mr. BRONKIE.** That slate be given a separate classification the same as granite, marble, talc, feldspar, vermiculite, and other competitive and comparative products.

**Senator TAFT.** It is not in the House bill?

**Mr. BRONKIE.** It is in the House bill, Senator, but it is tied to stone, and stone is a low cost, bulk product. Crushed stone you buy by the ton. Sand and gravel you buy by the ton at a very low figure. All it is is a question of having to go into a bank and dig it out with a steam shovel and put it on a truck. We have a very complicated and expensive development and exploration program to pay for, a big plant to carry. Our problem is exactly the same on a smaller scale, of course, as the oil industry or the copper mining industry or any other mineral product.

**Senator HOEV.** You want this put over into the other classifications?

**Mr. BRONKIE.** No. We just want it to be given its own name.

Your law reads now:

In the case of asbestos, sand, gravel, stone (including pumice, scoria and slate), brick and tile clay, shale, oyster shell, clam shell, granite, and marble, 5 percent,

**Senator HOEV.** What is it you want done? You

mentioned slate in the last. Do you want it mentioned separately?

Mr. BRONKIE. We want it mentioned separately, the same as marble and granite. We do not want it included in stone, because it is not competitive with stone or comparative with it.

[837] Senator MILLIKIN. Do you use the slate for anything but shingles?

Mr. BRONKIE. Yes, sir; we use it for very many products. Electrical switchboards is a very important use of it at the present.

Senator MILLIKIN. Give me more instances of what you do with it.

Mr. BRONKIE. I think we have it in this statement here:

*Uses.*—Slate is used in a variety of products: namely, natural roofing, roofing granules, siding, electrical switchboards, paints, ceramics, structural slate products, blackboards and bulletin boards, school slates, expanded aggregates, oilliard table tops, and has other numerous and miscellaneous uses important to the economy of the country, industrial and chemical.

Senator HOEY. Would you like to have this statement included in the record?

Mr. BRONKIE. Yes, sir.

Mr. HOEY. Mr. Chairman, I suggest that that be included in the record.

The CHAIRMAN. Yes. That will be included in the record.

(The statement referred to is as follows:)

Statement in Support of Percentage Depletion Allowance for Slate Producers by Independent Classification in Bill.

This statement is submitted in behalf of the slate

producers in the Vermont-New York, Pennsylvania-Maryland, Maine and Virginia slate districts. The slate industry has been overlooked heretofore in the development of the application of the concept of percent depletion. The following facts are submitted for your consideration in support of our claim.

#### FACTS

1. *Small business.*—The slate industry is composed of approximately 80 relatively small companies operating on low-profit margins.

2. *Industry location.*—Slate is a nonmetallic mineral product manufactured in various grades and types and in various States; namely, Vermont, New York, Pennsylvania, Virginia, California, Arkansas, Georgia, Maine, Maryland. Annual total production is about 800,000 tons with a total value of about \$12,000,000.

[838]

7. *Quality product.*—Slate is a specialized non-metallic mineral product currently having a market value ranging from \$10 to \$30 per ton. It should be classified independently as are marble, granite, quartzite, tripoli, etc. Definitely it should not be classified with low-cost bulk products such as stone, shale, sand and gravel that have values per ton only a fraction that of specialized slate products. [Italics supplied.]

[839]

#### USES OF SLATE

Slate is well-suited to engineering uses because of its high strength, low absorption, resistance to weathering and chemical attack, low electrical conductivity, uniformity of composition, and permanent stability

of dimension. Dimension slate or slab slate is used for roofing, electrical panels, architectural panels, laboratory fixtures, sanitary ware, blackboards and bulletin boards, flagstones, and miscellaneous uses. Slate granules are used chiefly in surfacing prepared roofing and siding. Slate flour is used as a filler in putty, wallboard, phonograph records, crayons, blotting paper, linoleum, \* \* \*

[861] Statement of A. C. FORD, Director of Sales, Southern Lightweight Aggregate Corp.

Mr. FORD. Mr. Chairman and gentlemen, my name is A. C. Ford, and I represent the Southern Lightweight Aggregate Corp., in Richmond.

\* \* \* Vermiculite lightweight aggregate has, for some time, received 15 percent depletion allowance, and the present tax bill already passed by the House of Representatives adds Perlite to the list of minerals to receive the same allowance. In order to permit an equitable allowance for competitive products we sincerely request that "slate when used in the manufacture of lightweight aggregate," the mineral used in the production of Solite, be included at the same figure.

\* Senator MILLIKIN. Is Solite a trade term?

Mr. FORD. Yes, sir.

[862] Senator MILLIKIN. Is it a term that is restricted to some particular outfit?

Mr. FORD. Yes. That is our trade name, Senator, for our material that is composed of lightweight aggregate that is made from slate when used in the production of lightweight aggregate.

Senator TAFT. We had a man here on all slate.

Mr. FORD. On all slate, yes, sir. But this is the "slate when used in the production of lightweight aggregate," which is very, very hard to find in this country at the present time.

Mr. FORD. The Southern Lightweight Aggregate Corp. produces a lightweight aggregate under the trade name of Solite, certain slaty minerals being used as the raw material for its manufacture. In the case of all three; Perlite, Vermiculite, and Solite, the raw material is expanded in certain heating equipment under high temperature, producing a lightweight aggregate suitable for the combination with portland cement to produce concrete products, such as structural concrete, roof slabs, buildings, building units, insulating concrete and precast shapes. The advantageous merits of lightweight aggregate are, the tremendous savings in steel, their high insulating qualities, their inertness, and durability.

[863] True slate is found in Maine, New York, Vermont, Pennsylvania, Maryland, Virginia, and Georgia, along our Atlantic seaboard, and also in Arkansas and California. Slate of this type is ideally suited for production of shingles and similar units. However, there is a distinct difference between the slate we use for the manufacture of our lightweight aggregate and that used for the production of slate shingles and other slate products.

In the slate we use the forces of nature have caused an altering, or softening, of the slate deposit for a depth of 50 feet. The slate in this altered condition is ideal for the production of lightweight aggregate.



This altered slate in our deposit is an extremely unusual occurrence.

\* \* \* \* \*

—House Hearings, 1953

(House Hearings, General Revenue Revision (1953).)

[2078] (The following material was submitted for the record on topic 38:)

House of Representatives,  
Washington, D.C., August 13, 1953.

Hon. DANIEL A. REED,  
Chairman, Ways and Means Committee, New House  
Office Building, Washington 25, D.C.

DEAR DAN: It is my understanding that on Friday, August 14, hearings will be held on item 38, depletion and exploration expenditures, and that the interested parties will be heard.

[2079] It is my wish to again express my interest in this and attach herewith memoranda pertaining to the subject which it is my desire to have incorporated as a part of the hearings.

Sincerely,

DEAN P. TAYLOR,  
Member of Congress.

## THE SLATE INDUSTRY

### INTRODUCTION

Slate is a metamorphic deposit, formed during earth disturbances of geologic time by the action of heat and pressure on shales and other finely divided sedimentary deposits. During this process secondary minerals were formed, principally mica, the crystals of which when properly orientated give to slate its outstanding characteristic of uniform cleavage. This

unusual feature, which is fully developed only in limited deposits of slate within the major slate districts of the United States, makes it possible to cleave slate in slabs for processing in various commercial forms.

[2080] FACTS

[2081]

7. Quality product.—*Slate is a specialized nonmetallic mineral product currently having a market value ranging from \$10 to \$50 per ton. It should be classified independently as are marble, granite, quartzite; tripoli, etc. Definitely it should not be classified with low-cost bulk products such as stone, shale, sand, and gravel that have values per ton only a fraction that of specialized slate products. [Italics supplied.]*

#### THE SLATE INDUSTRY—A SURVEY

[2083]

*Slate for roofing is by far the most important product derived from commercial slate. This industry has been active in the United States since the middle of the 19th century. [Italics supplied.]*

## SODIUM CHLORIDE (SALT)

(Percentage depletion, first allowed beginning with 1951)

Senate Hearings, 1951

(Senate Hearings, Revenue Act of 1951)

[908] Statement of LLOYD P. WEBRE, President, United Salt Corp.

*Salt is produced primarily in rock-salt form and in brine. The rock salt is produced very much the same way as coal or potash or limestone, and the equipment which is used to produce it is the same. [Italics supplied.]*

The units are used in all the mines and the same units exactly can be used for each purpose. In case of the production of brine, it is very similar to the process for producing sulfur, only we do not use any superheated steam; we use cold water. We just pump fresh water down into a salt deposit and force brine back.

[909]

For brine purposes, certain impurities can be removed from salt, *but from rock salt, the salt must be used as such and is not refined*, but is merely treated for human consumption. [Italics supplied.]

[910]

Upon the basis of the figures furnished, the yield per ton in the years listed has been as follows—these are Government statistics, also:

	Yield per ton
1947-----	\$3.25
1948-----	3.31
1949-----	3.47

These figures not only show a low return, but also demonstrate that salt as a commodity has not enjoyed the increase which has taken place in the realization upon other commodities. These figures include, of course, salt of all types and methods of production.

\* \* \* \* \*

[911]

\* \* \* \* \*

Upon the basis of statistics released by the Bureau of Mines in its 1949 Minerals Yearbook, the total value of *naked salt* produced in 1949 amounted to approximately \$54,000,000.. [Italics supplied.] Carried further, this figure may be translated into effect upon Federal income and excess profits taxes as follows:

Value of salt-----	\$54,000,000
Cost of mining, treatment, etc-----	27,000,000
Gross income from property-----	27,000,000
Percentage depletion, 15 percent-----	4,050,000

If it is assumed that the selling and general expenses, interest, and so forth, are 80 percent of the gross income from the property, and that the depletion allowance is limited to 50 percent of the net income from the property, the deduction would be as follows:

Gross income from property-----	\$27,000,000
Selling and general expenses, etc-----	21,000,000
Net income from property-----	5,400,000
Limitation at 50 percent-----	2,700,000

\* \* \* \* \*

[912]

Mr. WEBRE. When we say "naked salt," we mean the salt before it is packed, you see, and the average net plant after deduction of production costs, and then 15 percent of that, you see—

It is the most basic of all chemicals. It is used for caustic, chlorine, sodium, and there are just hundreds of things made from salt.

[1010] Statement of J. L. BAYLESS, Jr., President, Jefferson Island Salt Co., Louisville, Ky.

[1011] The most feasible way of providing this incentive is for the Federal Government to allow a percentage depletion on salt, comparable to the depletion allowed on similar minerals such as coal, oil, sulphur, phosphate, etc.

Based on statistics released by the Bureau of Mines in its 1949 Minerals Yearbook the total value of naked salt produced in 1949 amounted to \$54,048,226. Assuming a 50-percent cost of extraction, treatment, etc., for the industry, and a 15-percent percentage-depletion allowance, disregarding possible interim excess-profits taxes, the cost to the Federal Government of this depletion allowance would be only about 11½ million dollars per year. \* \* \*

[2390] Statement of E. J. BACHMAN, Vice President, Jefferson Island Salt Co., Louisville, Ky.

[2391] Based on statistics released by the Bureau of Mines in its 1949 Minerals Yearbook, the total value of naked salt produced in 1949 amounted to \$54,048,-



226. Assuming a 50-percent cost of extraction, treatment, etc., for the industry and a 15-percent percentage-depletion allowance, disregarding possible interim excess-profits taxes, the cost to the Federal Government of this depletion allowance would be only about \$1,500,000 per year. \* \* \* [Italics supplied.]

It is, therefore, recommended that Congress provide for a 15-percent percentage-depletion allowance on salt by including the word "salt" in section 114(b) (4) of the Internal Revenue Code of 1950 between the words "rock asphalt" and "phosphate rock."

House Hearings, 1953

(House Hearings, General Revenue Revision (1953))

[2043] Statement of DANIEL PETERKIN, Jr., Member, Executive Committee of Salt Producers Association, and President of Morton Salt Co., Chicago.

Mr. PETERKIN. Mr. Chairman and members of the committee, my name is Daniel Peterkin, Jr. I am president of the Morton Salt Co. of Chicago, and I am appearing here on behalf of the Salt Producers Association.

[2044]

Most of the deposits are worked by wells. Water is forced down, and the resulting *brine is evaporated*. In other deposits the salt is mined. [Italics supplied.]

[2046] The CHAIRMAN. I would like to ask you one question. As I understand in salt mining, you force hot water down into the shafts and then pump the salt water out and evaporate it; is that correct?

Mr. PETERKIN. Except that the water need not be hot. The water is forced down by air pressure, which lifts out the brine. It is brought up as brine and evaporated.

Mr. READ. And salt is also mined. Both systems are used.

Mr. PETERKIN. *Both are used; dry salt is mined, and evaporated salt is produced from brine method.* [Italics supplied.]

\* \* \* \* \*

### STONE

(See "LIMESTONE: ALL GRADES . . . PLUS OTHER STONES . . .",  
*supra*, pp. 363-381.)

### SULPHUR

(Percentage depletion first allowed beginning with  
1932)

House Hearings, 1932

(House Hearings, Revenue Revision (1932))

[337] Statement of E. T. CUMMINS, Washington, D.C., representing domestic sulphur producers.

Mr. CUMMINS. Mr. Knoblock has asked me to represent him and present certain matters to this committee in which we are jointly interested.

Mr. CRISP. You represent whom?

Mr. CUMMINS. I represent one of the sulphur companies interested in the matter, the Freeport Sulphur Co.

The Freeport Sulphur Co., the Texas Gulf Sulphur Co., and the Duval-Texas Co. ask you to make a slight amendment to section 114(b)(3) of the 1928 revenue act, which deals with depletion of mines, or particularly the oil and gas section of that provision.

[338] (The brief is as follows:)

**BRIEF ON BEHALF OF SULPHUR PRODUCERS**

**CHAIRMAN, WAYS AND MEANS COMMITTEE,  
House of Representatives of the United States.**

DEAR SIR: The following brief is submitted on behalf of the Freeport Sulphur Co., Texas Gulf Sulphur Co., and Duval-Texas Sulphur Co., being all of the producers in the United States of sulphur by the Frasch process; that is, recovery through driven wells. *They represent in excess of 99 percent of the total production of sulphur in the United States.* (See Mineral Industry, 1930, p. 560.) [Italics supplied.]

These producers unite in requesting an amendment to section 114(b)(3) of the revenue act of 1928 so as to include sulphur in the percentage depletion granted to oil and gas wells.

\* \* \* \* \*

[339] I. The mining and production of sulphur by the Frasch process by using drilled wells renders this mining operation more similar and analogous to oil and gas wells than to metal mining

The Frasch process of mining sulphur (under which over 99 percent of the production in the United States is obtained) is:

First, to sink a well into the caprock which overlies the rock salt core of the salt dome in which these deposits of sulphur occur. These wells are drilled with a rotary rig similar to that employed in the petroleum industry for work in soft formations. Second, into this same well is pumped water heated under pressure to a temperature above the melting point of sulphur. This melts the sulphur in situ. Third, it is then pumped to the surface by compressed air. The sulphur arrives at the surface in a liquid form.

Fourth, it is then distributed into bins where it is allowed to solidify, for immediate sale and distribution. *The sulphur so recovered is in excess of 99.5 percent pure and is of the grade used in commerce. It requires no further treatment or refining to prepare it for the trade. [Italics supplied.]*

The derricks and drilling rigs are identical with those used by oil producing companies and the sulphur dome in operation presents almost the appearance of an operating oil field.

Oil, gas, and sulphur are all discovered and recovered by sinking wells and bringing the deposit to the surface. In some cases natural pressure brings the oil to the surface. In other cases it has to be aided by either pumps or artificially induced pressure, as in sulphur.

**II. Similar to oil and gas sulphur is a commercial product at the mine and does not have to be subjected to a further treatment for sale**

Sulphur, like oil and gas, has a value as it comes out of the ground. Similar to oil and gas there is an established field price for sulphur which indicates directly [p. 340] the income from the property. In the case of ores of the metals there is no general field price for the ore at the mine and when the taxpayer does his own concentrating, smelting, refining, transporting and marketing, all that is known is the selling price of the refined or final product. Contrasted with this situation of the ores of the metals sulphur, oil, and gas have a field price and no profit derived from the process of their further treatment could be the subject of depletion.

*Percentage depletion, therefore, is peculiarly appropriate for sulphur, together with oil and gas wells, and avoids the difficulty existing in the case of metal mines of allocating the proper portion of the income between that which was due to the mining operations*

*simpliciter and that which was due to smelting, refining, transporting, etc.* [Italics supplied.]

[341] VI. Numerous tax questions arising out of the distribution of depletion dividends will be avoided

We base this application upon the close association of ownership and discovery between sulphur and the oil and gas wells, the multiple nature of the various interests in the sulphur domes and the unique method of producing and mining sulphur, essentially similar to that of producing oil and gas, and *the fact that there is for sulphur, as for oil and gas, a field price that avoids any allocation in determining the income to which percentage depletion is applicable.* [Italics supplied.]

#### Summary of Advantages

All of which facts we submit warrant the classification of sulphur producers of this country for depletion with the oil and gas industry.

Respectfully submitted.

H. F. J. KNOBLOCH.

E. T. CUMMINS.

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1604] Statement of the Honorable CLARK W. THOMPSON, a Representative in Congress from the State of Texas.

[1607] THE MINING AND PRODUCTION OF SULFUR BY THE FRASCH PROCESS

The Frasch process of mining sulfur (under which over 98 percent of the production in the United States is obtained) is:



First, to sink a well into the cap rock which overlies the rock-salt core of the salt dome in which these deposits of sulfur occur. These wells are drilled with a rotary rig similar to that employed in the petroleum industry for work in soft formations. Second, into this same well is pumped water heated under pressure to a temperature above the melting point of sulfur. This melts the sulfur in situ. Third, it is then pumped to the surface by compressed air. The sulfur arrives at the surface in a liquid form. Fourth, *it is then distributed into bins where it is allowed to solidify, for immediate sale and distribution. The sulfur so recovered is in excess of 99.5 percent pure and is of the grade used in commerce. It requires no further treatment or refining to prepare it for the trade.* [Italics supplied.]

\* \* \* \* \*

TALC

(Percentage depletion first beginning with 1944)

House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

[25] Statement in support of percentage depletion for talc producers before the Ways and Means Committee of the House of Representatives, June 4, 1947.

My name is Henry Mulryan of Glendale, Calif. \* \* \*

\* \* \* \* \*

[26] MINING, MILLING, AND PROCESSING

Practically all of the talc mined in the United States is from underground operations. The mining of talc is comparable to the mining of other hard rock minerals, and in some instances presents exceptional hazards and difficulties which may not only

greatly increase costs but actually threaten the loss of the mine entirely.

Where highly specialized grades are desired, the ore itself is selected by hand before being sent to the mill for processing. After the crude ore is received at the mill, it is *crushed, pulverized* and bagged. The type of mill used for the milling depends upon the physical characteristics of the tale and its ultimate use. Increasing amounts are being micronized, as the fineness of the material greatly influences the end to which it can be put. One company uses a flotation plant for processing special grades and other producers have given serious thought of installing similar units. [Italics supplied.]

[34] Statement of Mr. HENRY MULRYAN, Los Angeles, Calif., representing the tale interests.

[36] Mr. REED. Do you find this tale being fine or does it have to be ground from rock?

[37] Mr. MULRYAN. It occurs as a mass of material. All of the material has to be ground in special equipment to very rigid specification before it can be used in the industry.

Mr. REED. You do not find it in beds like you would sand?

Mr. MULRYAN. No.

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[431]

Statement of S. W. Tuttle, Vice President and Secretary, International Tale Co., Inc., New York, N.Y.

I would like to describe briefly the operations engaged in by my company and by other talc companies which influenced the Congress to grant us this depletion allowance. \* \* \*

[432]

\* \* \* When the ore arrives at the mill it is put through the mill in a continuous process where it is *crushed and ground* to the specifications required by the consumer. [*Italics supplied.*]

The ground talc is bagged and ready for sale to the consumer. Most talc sales are made by the producing companies directly to the ultimate consumer. For instance, the annual tonnage of International Talc Co. of approximately 50,000 tons, is divided among consuming industries according to our sales records as follows: 65 percent paint, 20 percent ceramic, 5 percent paper, 3 percent rubber, 3 percent plastic, 2 percent textiles, 2 percent miscellaneous.

[434]

At this point I would like to bring up one other matter. The Treasury Department here is urging this committee and the Congress to decrease the percentage-depletion allowance for talc from 15 percent to 5 percent. For my company, the Treasury Department has not been content to wait for the Congress, but has undertaken to do this in an administrative manner. Notwithstanding the fact that for the last 57 years my company has sold talc from the Gouverneur and it has been accepted by the trade as talc, the Treasury Department, in its examination of our last returns has allowed us percentage depletion only on that part of our product which it character-

izes as chemically pure talc, thereby cutting down our percentage depletion to a great degree.

There is no such thing in the United States as chemically pure talc and we so stated in our brief before this committee at prior hearings. The Treasury action is in direct conflict with the action of the committee in its award of percentage depletion to commercially marketable talc in 1943 and in 1947. Even the transportation companies have, during this long period of time, established freight tariff recognizing *our product as ground talc*. At no time in the presentation to the committee either in 1943 or 1947 did we profess to mine, mill, or sell chemically pure talc but on the contrary, we specifically designated our product as *commercial talc*. Nor was the Treasury Department satisfied with this contention. It has gone further and is maintaining that the ordinary processing which I have described in this paper is not an ordinary treatment process as described by the statute. [Italics supplied.]

[491] Statement of HENRY MULRYAN, Glendale, Calif.

My technical training is that of a mining geologist, having graduated from Stanford University in 1924. Since that time I have been engaged exclusively in the nonmetallic-mineral industry.

At the present time I am the executive vice president and general manager of the Sierra Talc & Clay Co., which company operates 14 mines in the States of California, Nevada, New Mexico, and Montana.

[492] In general, *talc*, a nonmetallic mineral, sells at a relatively low cost. The costs of operation are high in comparison with the sales price. And a part

of the reason for the low price is due to high transportation rates from the mine to the mill to the ultimate consumer who might be any place in the United States. Further reasons for low price levels and small margins of profits are the highly competitive conditions existing between talc producers. [Italics supplied.]

Statement of A. PRESCOTT LOOMIS regarding percentage depletion for talc.

[2892] All the talc mined and milled in the Gouverneur district of New York State, is essentially of a similar character of good white color, both fibrous and granular in structure. The main productive region lies in Talcville and Fowler, N.Y., a few miles from Gouverneur, in St. Lawrence Country. The ore bodies lie at mining depths of sometimes about 900 feet. The mining of talc is as difficult and expensive as metal mining. The type of mining is known as stope mining. Considerable exploration and development work is necessary before mining the ore. The ore is wet drilled and blasted with dynamite. The broken ore is sorted as to grades, granular or fibrous, and also as to oil absorption properties. In other words some types of ore are heavy and others light. The sorted ore is blended and loaded into mining cars underground and transported to the mine shaft at which point it is loaded into mine skips and hoisted to the surface where it is dumped into trucks for transportation to the mills a few miles away. There is a constant danger of flooding of the mines and it is necessary to constantly keep pumps operating to keep the water out. When the ore arrives at the mill it is put through the mill in a continuous process where it is *crushed and ground* to the specifications required



by the consumer. [Italics supplied.] The ground talc is bagged and ready for sale to the consumer. Most talc sales are made by the producing companies directly to the ultimate consumer. For instance, the annual tonnage of International Talc Corp. of approximately 50,000 tons, is divided between consuming industries according to their sales records as follows:

	Percent		Percent
Paint.....	65	Plastic.....	3
Ceramic.....	20	Textiles.....	2
Paper.....	5	Miscellaneous.....	2
Rubber.....	3		

Senate Hearings, 1950

(Senate Hearings, Revenue Revisions of 1950)

[790] Statement of WESLEY E. DISNEY regarding clarifying amendments to section 204 of H.R. 8920.

[791] Talc has many industrial uses but *there is little or no market for it in its crude form. It must be crushed and ground before it can be sold.* To eliminate any further controversy with the Bureau, I suggest that section 114(b)(4)(B) of the Internal Revenue Code which defines ordinary treatment processes be amended by inserting "talc" after the word "potash" in subsection (iv) so that talc will be listed among those ores which are not customarily sold in the form of the crude mineral product. *Just as in the case of copper, fluorspar, and other ores, talc has no market until after the ordinary crushing and grinding processes have been applied.* \* \* \* [Italics supplied.]

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1584] Statement of S. W. TUTTLE, Vice President and Secretary, International Talc Co., Inc., New York.

Mr. TUTTLE. My name is S. W. Tuttle, vice president and secretary of the International Talc Co., Inc., with main offices located at 41 Park Row, New York, N.Y. We are one of the three talc-producing companies in the Gouverneur mining district of New York State.

[1585] \* \* \* The ore is wet-drilled and blasted with dynamite. The broken ore is sorted as to grades, granular or fibrous, and also as to oil-absorption properties. In other words, some types of ore are heavy and others light. The sorted ore is blended and loaded into mining cars underground and transported to the mine shaft at which point it is loaded into mine skips and hoisted to the surface where it is dumped into railroad gondolas for transportation to the mills a few miles away.

There is a constant danger of flooding of the mines and it is necessary to constantly keep pumps operating to keep out the water. When the ore arrives at the mill it is put through the mill in a continuous process where it is *crushed and ground* to the specifications required by the consumer. [Italics supplied.]

The *ground talc* is bagged and ready for sale to the consumer. Most talc sales are made by the producing companies directly to the ultimate consumer. For instance, the annual tonnage of International Talc Co. of approximately 50,000 tons, is divided among consuming industries according to our sales records as follows: 65 percent paint, 20 percent ceramic, 5 percent paper, 3 percent rubber, 3 percent plastic, 2 percent textiles, 2 percent miscellaneous. [Italics supplied.]

[1586] I want to say that the talc industry is a small industry. The total tonnage mined by all of the talc

companies in this country is only some 350,000 tons, and it is a high-cost operation.

\* \* \* \* \*

House Hearings, 1953

(House Hearings, General Revenue Revision (1953))

[2033] Statement of HENRY MULRYAN, President, Sierra Talc & Clay Co., South Pasadena, Calif.

\* \* \* \* \*

[2035]

\* \* \* \* \*

The crude ore must be *crushed, ground*, and bagged. Conventionally, the talc taken from the mine is first crushed in primary and sometimes in secondary crushers to minus one-half inch material. Fine grinding is then achieved in tube mills, roller mills, hammer mills, mills using fluid energy, Raymond mills, and Hardinge mills, using closed circuits with Sturtevant, Raymond, or other types of air separators. [Italics supplied.]

*Although no blending, concentration, or other beneficiation is required*, with the exception of a single operation in Vermont, *talc must be ground to be salable*. There is attached as exhibit A the specifications of products sold by Sierra Talc & Clay Co., which products cover all commercial uses. These specifications demonstrate that *talc ore must be finely ground in order to be salable*. Substantially all talc sales are made by the mine operator directly to the ultimate consumer. *There is practically no commercial use for the raw ore until it has been finely ground*. As shown by the respective Mineral Yearbooks of the United States Bureau of Mines, in 1941, 89 percent; in 1943, 92½ percent; in 1948, 97 percent; and in 1950, 89 percent of the total United States

production of talc was required to be finely ground prior to the original sale. [Italics supplied.]

In other words, these grinding processes are not only the ordinary, normal practice of talc-mine operators; they are practically the universal rule. \* \* \* [2036]

\* \* \* \* \*

The CHAIRMAN. Pardon me. Not only in the face of the statute itself, but without grinding you could not sell the talc in your State?

Mr. MULRYAN. That is correct. *Practically all of it has to be fine ground to be marketable.* [Italics supplied.]

The CHAIRMAN. If it is not allowed to be ground, depletion is of no value to you?

Mr. MULRYAN. We would be out of business.

The CHAIRMAN. Thank you.

\* \* \* \* \*

[2037]

\* \* \* \* \*

We therefore ask that section 114(b)(4)(B)(iv) be amended to add "talc" to the list of minerals now contained in that subsection. We think this addition would make clear that Congress intended in section 114 that in the case of talc which is not customarily sold in its crude form, the term "ordinary treatment process" includes crushing and all grinding *necessary to bring the product to a commercially marketable state.* We think that is precisely what the law says today and what Congress intended, because when the law was amended in 1947 to include talc on a permanent basis, Congress acted in the light of testimony by the industry which showed clearly that talc is not customarily sold in its crude form, and that it must

undergo fine grinding to get it into a marketable state.  
[Italics supplied.]

[2041] Mr. MULRYAN. I would like to add, or to emphasize, that *until the talc is finally ground it has very little commercial use.* [Italics supplied.]

The CHAIRMAN. Mr. Mulryan, when you say that talc is not customarily sold in the crude state, is it my understanding that it is not considered a commercial product until it is ground fine for use?

Mr. MULRYAN. If you will refer back to the first paragraph on page 3, I quote from the Minerals Yearbook showing that certain percentages were sold.

The CHAIRMAN. Yes.

Mr. MULRYAN. Showing that in 1 year about 10 percent, or even as low as 3 percent was sold in the crude form.

The CHAIRMAN. I just wanted to clear that up, that it is not customarily sold in the crude form.

Mr. MULRYAN. That is correct.

The CHAIRMAN. And you have given the percentages, which is in 1 instance 10 percent.

Mr. MULRYAN. That is right.

The CHAIRMAN. Sold in the crude state.

Mr. MULRYAN. That is correct.

Mr. MULRYAN. The final pulverization, making the talc fine, is a part and parcel of the operation of making the talc commercially usable.

[2042] Mr. SIMPSON. But you say there is no market, that is, no substantial market of the product between the initial crushing and the pulverization process.

Mr. MULRYAN. I would go further, and I would say



there is no market for it at that point, that is, between the crushing and the pulverization point.

Mr. SIMPSON. And do you further claim that that is a part of the mining process which must be done in order to make it commercially usable?

Mr. MULRYAN. That statute is very clear and states the ordinary process that should apply. But it is the Treasury Department which has promulgated a new regulation on July 18, excepting the words "*fine pulverization.*" *That is the normal process, in the processing of talc as it is obtained from the mine.* [Italics supplied.]

Mr. SIMPSON. And the amendment you want would do what?

Mr. MULRYAN. We want to clear up the situation so that the word "talc" will occur at the proper place in section 4, where it can be spelled out that the final grinding is an ordinary part of the treatment. \* \* \*

#### THENARDITE

(Percentage depletion first allowed beginning with 1947)

House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

[29] Statement in support of 15 percent percentage depletion for thenardite, before the Ways and Means Committee, House of Representatives, June 4, 1947.

#### DESCRIPTION AND OCCURRENCE

Thenardite is a nonmetallic mineral commonly known as sodium sulfate. It occurs in natural deposits, *some of which are in solution in brines and require processing.* It is found principally in the Western States of California, West Texas, Wyoming, Utah, Nevada, Montana, and Washington. Salt cake,

the manufactured form of sodium sulfate, is produced chiefly in Michigan, Ohio, and Pennsylvania. It occurs in many foreign countries, including Canada, England, Germany (Soviet zone), and Chili. [Italics supplied.]

#### PRODUCTION AND PROCESSING

Natural salt cake is processed from natural deposits, and different degrees of processing are required depending upon impurities and other chemicals contained therein. Some natural production is obtained by *evaporation*. Byproduct salt cake is produced principally in the manufacture of hydrochloric acid. Substantial quantities are imported. (See appendix.) The tabulation in the appendix shows that annual production of natural sodium sulfates is valued at  $11\frac{1}{2}$  million dollars. A reasonable estimate of annual dollar value for byproduct salt cake would be somewhere between 8 and 10 million dollars for the 5 years ending 1945. [Italics supplied.]

The cost of production varies considerably, depending upon impurities and other chemicals contained in the natural deposits or brines. It is a very competitive product, and you will note that over the 5 or 6 years for which statistics are furnished in the appendix, *the value per short ton at producing plants is under \$10 per ton*. Ordinarily it cannot be shipped very far on account of freight rates being prohibitive. There are some instances where the freight charges [30] amount to as much or more than the value of the salt cake at the producing point. The producer invariably sells to the ultimate consumer. [Italics supplied.]

## (House Hearings, Revenue Revision of 1950)

[2894] Statement regarding percentage depletion for thenardite by American Potash & Chemical Corp., Searles Lake, Calif.

\* \* \* \* \*

Thenardite is a sodium sulphate, commonly known as Glauber's salts or salt cake. It is usually found in pre-historic oceanic lake beds.

Thenardite has a variety of uses. It is extremely important in the production of wood pulp for craft papers, especially in the southern part of the United States where the paper without the use of thenardite would be too dark for commercial uses. It is important as a mineral stock feed, as a detergent for soap purposes, cleansers, and toiletries. It is used in the glass industry as well as in the sugar industry. It is important in the production of dyestuff and in the mining and mineralogical industry as a flux. It will probably become important in the near future in the manufacture of fuels for jet engines.

The gross production of thenardite in 1934 was 8,192 tons, with a gross value of \$20,573. In 1949, after percentage depletion was allowed by the 1947 statute, the production rose to 139,334 tons with a gross value of \$1,886,016.

American Potash & Chemical Corp. is engaged at Searles Lake, Calif., in the production of potash, trona, borax, and thenardite, having in 1949 completed a plant at a cost of \$5,500,000. In 1949 we spent over \$250,000 inside the plant to expand our facilities to produce thenardite alone. We embarked on an entirely new project on Searles Lake for additional production of thenardite which at the time was in extremely short supply.

[2895] *The production of thenardite consists in supplying brine into the air during the winter when the temperature is less than 45°. Glauber's salts separate out at this temperature. In warmer weather we harvest the Glauber's salts from the lake surface, sludge it into the plant, and refine it into thenardite. [Italics supplied.]*

[2895] Prices to the consumers of thenardite have been lowering. In 1948 the per-ton price was \$14; in 1950 it is \$10.50.

In our plant at Searles Lake we must produce all four of the projects above mentioned. In effect the trona operation would not be economical unless we produce all four major projects—potash, borax, trona, and thenardite.

#### TRONA

(Percentage depletion first allowed beginning with 1947)

House Debate, 1947

(93 Cong. Record (Part 8), 80th Cong., 1st Sess. (1947))

[9629]

Mr. BARRETT. I want to congratulate the gentleman for bringing in this bill and may I say to him that I think the percentage depletions allowed in this bill are very fair and will be quite helpful in the development of these minerals in the West. I want to say to the gentleman, however, that we have a new development in our State, the mining of trona. *It is quite similar to thenardite in this bill.* The company presently operating has spent in excess of a million dollars in

the development of this mine, building a shaft, and so forth. They must go deep into the ground in order to take out this mineral. It is an entirely new industry in our State. *It is used for the same purpose as thenardite.* It will be developed mainly on the public domain and bring income to the Treasury of the United States by reason of the royalties paid. I am hopeful that it too could be accorded the same percentage depletion as is granted to these other minerals in this bill. [*Italics supplied.*]

#### VERMICULITE

(Percentage depletion first allowed beginning with 1944)

Senate Hearings, 1943

(Senate Hearings, Revenue Act of 1943)

[839] Senator WALSH. A memorandum for inclusion in the record has been submitted by Mr. A. T. Kearney of the committee of vermiculite miners which will be inserted in the record at this point.

(The memorandum referred to is as follows:)

#### [842] MEMORANDUM REGARDING PERCENTAGE DEPLETION FOR VERMICULITE

[843] 7. *Fabricators and distributors of vermiculite products.*—The marketing of vermiculite products embraces three stages. *The ore is mined and sold by the [844] mining companies to fabricators or processors in various parts of the United States.* They subject it to a heat-treating process that expands the ore into loose granular form. The fabricators and processors either sell the expanded material to dealers or use it in the fabrication of mixed,



formed, and fabricated products containing vermiculite. The dealers, in turn, sell to the consuming public. [*Italics supplied.*]

There are today approximately 35 fabricators and processors in the United States. There are approximately 4,000 dealers. \* \* \*

[844] 8. *Effect of proposed legislation on tax revenue.*—If 15 percent depletion were permitted to vermiculite miners, the estimated reduction in taxes for 1942 would have been \$32,002.70. As against this loss of revenue, there would be a substantial gain in revenue from fabricators, processors, and dealers. \* \* \*

#### House Hearing, 1947

(House Hearing, Percentage Depletion (1947))

[42] Statement of JOHN BISHOP, Chicago, Ill., representing the vermiculite interests. \* \* \*

[43] I would like to make a short statement and to file a brief which I have handed to each member of the committee, and I would like permission to have the brief inserted in the record.

Mr. REED. Without objection the brief will be inserted in the record.

(The document referred to is as follows:)

#### MEMORANDUM ON PERCENTAGE DEPLETION FOR VERMICULITE

#### Foreword

Vermiculite, a nonmetallic mineral used principally for insulation, lightweight aggregates, and plaster was granted percentage depletion of 15 percent of gross

income in 1943, the allowance to continue until the termination of hostilities in the then war.

## I. HISTORY OF THE VERMICULITE INDUSTRY

### (a) *Description and location.*

Vermiculite is a nonmetallic mineral. Chemically, it is an aluminum magnesium silicate. \* \* \*

### (c) *Mining and milling.*

Mining for vermiculite is done principally in open pits with power-driven equipment, or in tunnel with pick and shovel.

[44] Milling is quite complicated. The processes used vary with the different mines. *Air separation is used on some properties. In others, screening and drying are adequate to produce a marketable concentrate.* Because of the different minerals with which vermiculite in place is associated, it has been necessary for each miner to develop a process that is suitable for his particular deposit. There has never been and is not now any standardized process or equipment for milling vermiculite. [Italics supplied.]

### (d) *Uses of vermiculite.*

*The product which is derived from the mining and milling operation is vermiculite concentrate.* As such, it has no commercial use. *In concentrate form it is sold to processors and fabricators.* The latter subject it to a heat-treating process that expands the mineral in a manner comparable to the popping of corn. In its expanded form it becomes a commercial product. [Italics supplied.]

Among the products presently being manufactured from vermiculite are the following:

The above list is not exhaustive. It merely illustrates the wide range of uses to which the material

is being put. Vermiculite is today an accepted commercial product in a field that was unknown 15 years ago. In many of its uses, it performs functions that no other known material is capable of performing.

• (e) *Marketing of vermiculite and vermiculite products.*

The marketing of vermiculite embodies three stages: (1) *The sale of the concentrate to the processors and fabricators*; (2) the processing and sale of the expanded material and fabricated products to dealers; and (3) the sale of the finished product by the dealer to the consuming public. [Italics supplied.]

In the United States today there are 8 miners, approximately 35 processors and fabricators, and approximately 15,000 dealers. \* \* \*

Vermiculite is the basic mineral from which the income of processors, fabricators, and dealers is derived. In this respect, it is comparable to iron, copper, or lead sold by mine owners or operators to furnaces and smelters. Just as the ores are sent to furnaces and smelters whose products are in turn sold to fabricators for the manufacture of countless articles of commerce, *so vermiculite is sold to processors and fabricators to make therefrom a large variety of commercial products.* [Italics supplied.]

Basic metals such as iron, copper, and lead are permitted percentage depletion. Vermiculite occupies the same position in the nonmetallic industry. It should therefore be accorded the same depletion.

#### [45] IV. THE ARGUMENT FOR PERCENTAGE DEPLETION FOR VERMICULITE

[50] 5. *The rate for vermiculite should be the same as that allowed metal mines.*

(a) *The mining, processing and marketing of vermiculite is comparable to metal mining.* \* \* \*

(2) \* \* \*

Vermiculite ore is found in association with other rock, such as syenite or pyroxenite. It contains a high-moisture content. *To concentrate it, it is necessary to dry, crush, and screen the crude ore and then put it through an air-separation process.* It equals in complexity the concentration process in metal mining. [Italics supplied.]

[51] Respectfully submitted.

BLACK MICA MINES, INC.,  
BEE TREE VERMICULITE MINES, INC.,  
UNIVERSAL ZONOLITE INSULATION CO.,  
ALEXITE ENGINEERING CO.

[53] Mr. BISHOP. Vermiculite is one of the non-metallic minerals. It is found in North and South Carolina, Texas, Wyoming, Montana, and Colorado. When mined, it is shipped to manufacturers and fabricators who subject it to a high degree of heat and in that process it expands, something like the popping of corn.

In its expanded form it becomes a commercial product.

There are today 8 miners, 35 processors or fabricators, and approximately 15,000 dealers in the United States. The production for 1946 [54] was approximately 82,000 tons, having a value of approximately \$793,000. For the same period, the sales of expanded vermiculite by processors was approximately \$5,537,000, and by dealers, approximately \$6,645,000.

The principal point that the vermiculite industry makes in its argument for percentage depletion is the one that has been mentioned by some of the previous

witnesses; and that is, if it is not granted percentage depletion it would be discriminated against in favor of the metal mines and other nonmetallics such as sulfur and potash.

House Hearings, 1950

(House Hearings, Revenue Revision of 1950)

[413] Statement of John H. Bishop, Chicago, Ill., representing miners of vermiculite.

(The prepared statement of Mr. Bishop follows:)

Statement of JOHN H. BISHOP.

I. HISTORY OF PERCENTAGE DEPLETION FOR  
VERMICULITE

Vermiculite, a nonmetallic mineral, was first granted percentage depletion of 15 percent of gross income in the Revenue Act of 1943. This allowance was made during the war and hence was on a temporary basis. The grant was terminated by Presidential proclamation at the end of 1946. In 1947 Congress, after a study of the problem and after hearings before the Ways and Means Committee, fixed the percentage depletion allowance of vermiculite on a permanent basis at 15 percent of gross income, the allowance, however, not to exceed 50 percent of net income.

III. ARGUMENT FOR RETENTION OF PERCENTAGE DEPLETION AT 15 PERCENT OF GROSS INCOME FOR  
VERMICULITE

[414] A review of the situation today will show that the conditions which prompted Congress to grant per-



centage depletion in 1947 still exist today. Let us review them briefly:

1. *The allowance will benefit both the miners and the Treasury.*

In hearings before the Ways and Means Committee in 1947, the vermiculite miners argued that if they were granted percentage depletion the industry would be so stimulated that increased rather than reduced revenues would result. The record since the grant of percentage depletion proves conclusively that the argument then presented was correct.

In 1943, the year prior to the first percentage depletion allowance for vermiculite, 46,645 tons of vermiculite were mined and shipped. Tonnage mined and shipped since 1943 is as follows:

	Tons		Tons
1944-----	54, 116	1947-----	131, 385
1945-----	64, 808	1948-----	138, 635
1946-----	86, 390	1949 (estimated)-----	168, 000

Tax revenues from miners during these years are estimated as follows:

1944-----	\$72, 000	1947-----	\$106, 000
1945-----	73, 000	1948-----	188, 000
1946-----	96, 000	1949-----	300, 000

*Vermiculite is a basic mineral which is sold in its crude or concentrated form to processors who exfoliate it and from the processed mineral fabricate many different types of materials, all of which are sold through dealers. The income from the industry, therefore, is derived from three sources: the miners, the processors, and the dealers. [Italics supplied.]*

*Vermiculite ore in its concentrated form sells for approximately \$10 per ton. [Italics supplied.] Exfoliated vermiculite that is sold by processors brings approximately \$75 per ton. It is estimated that the mark-up of the dealers over the processor's price is 20 percent. On this basis gross sales by miners,*

processors, and dealers for the last 4 years are estimated as follows:

[415] 3. *The rate should be the same because the conditions are the same.*

(a) *The mining, processing, and marketing of vermiculite are comparable to metal mining.*— \* \* \*

Vermiculite mining, processing, and marketing embrace essentially the same operations. Thus:

1. The ore is mined in substantially the same way.

[416] 2. The concentrating process is equally as complicated as that used in metal mining.

Vermiculite ore is found in association with other rock, such as syenite or pyroxenite. It contains a high moisture content. *To concentrate it, it is necessary to dry, crush, and screen the crude ore and then put it through an air-separation process.* It equals in complexity the concentration process in metal mining. [Italics supplied.]

House Hearings, 1951

(House Hearings, Revenue Revision of 1951)

[1612] Statement of JOHN H. BISHOP, Attorney, Chicago, Ill.

Mr. BISHOP. Mr. Chairman and members of the committee, I am appearing here on behalf of the miners of vermiculite, one of the nonmetallic minerals, and I am going to ask leave to incorporate in the record a statement which I have prepared and then very briefly to summarize it. \* \* \*

\* \* \* Vermiculite is what we call a basic mineral in that it is mined in its crude form and then is proc-

essed, and under the processed mineral many products are made. So when we come to consider the question of tax revenue we consider it as coming from *the miners*, from the processors, and from the dealers. \* \* \* [Italics supplied.]

[1613] (The statement referred to follows:)

MEMORANDUM ON PERCENTAGE DEPLETION FOR  
VERMICULITE

[1615] Since those estimates were made, another year's figures have become available. The trend indicated for previous years carried into 1950. The following table indicates the estimates for the year 1950 [italics supplied]:

Tonnage mined.....	212, 000
Sales by miners <sup>1</sup> .....	\$2, 120, 000
Sales by processors.....	15, 900, 000
Sales by dealers.....	19, 680, 000

<sup>1</sup> Bureau of Mines Yearbook fixes \$10 a ton as the price of ore and \$75 a ton as the price of expanded vermiculite.

\* \* \* In this connection, we must keep in mind that vermiculite is *a basic mineral which is sold in its crude or concentrated form to processors who expand it and from the processed mineral fabricate many different types of materials, all of which are sold through dealers.* The income from the industry, therefore is derived from three sources—the miners, the processors, and the dealers. [Italics supplied.]

Since the depletion allowance relates only to miners, it is at once apparent that the taxes to be paid by processors and dealers would in no way be affected. And of the three classifications, the miners pay the smallest amount of tax. \* \* \* [Italics supplied.]

[1617] Respectfully submitted.

AMERICAN VERMICULITE Co.,

*Spruce Pine, N.C.*

ZONOLITE Co.,

*Libby, Mont.*

MIKOLITE Co.,

*Encampment, Wyo.*

\* \* \* \*

#### WOLLASTONITE

(Percentage depletion first allowed beginning with 1951)

Senate Hearings, 1951

(Senate Hearings, The Revenue Act of 1951)

[895] Statement of FRED C. FERNALD, General Counsel, GODFREY L. CABOT, INC., accompanied by Charles A. Stokes.

\* \* \* \*

[896] This is the statement of Godfrey L. Cabot, Inc., before the Finance Committee of the United States Senate in support of proposal to add wollastonite to the list of minerals subject to 15 percent depletion under Section 114(b)(4)(A) of the Internal Revenue Code.

\* \* \* \*

*Wollastonite is a nonmetallic mineral being mined and marketed today. This calcium metasilicate (CaSiO<sub>3</sub>) has been used in floor and wall tile, welding rod coatings, alloying agents, and soil conditioners. It is white in color, brittle, and with a fibrous cleavage. It can be produced in large quantities and through milling it is prepared for use in industry. [Italics supplied.]*

Its use pattern is similar to that for talc which is already subject to the 15-percent depletion under section 114(b)(4)(A) of the Internal Revenue Code.

[897] Senator BUTLER. Is it classified as highly critical?

Mr. STOKES. Well, it cannot be classified as highly critical because *the material is not now in commercial production other than in a very small way, and this is a newly developing industry.* [Italics supplied.]

Senator BUTLER. How long has it been known by this name?

Mr. STOKES. The wollastonite mineral has been known probably for 20 or 30 years. The beginning use of wollastonite is only in the last 5 or 6 years, beginnings of the development, that is.

Senator KERR. It is a nonmetallic mineral?

Mr. STOKES. Yes, sir.

The CHAIRMAN. All right, you may proceed.

Senator MILLIKIN. What other minerals does it resemble?

Mr. STOKES. It resembles most closely in its use the talc minerals, pyrophyllite, steatite, and other forms of talc. They are magnesium silicates. This is a calcium silicate.

[899] Mr. FERNALD. \* \* \*

Mr. Chairman, I believe we have permission for Dr. Stokes to read a short statement which he has prepared, which elaborates a little on mine.

Mr. STOKES. My name is Charles A. Stokes. Gentlemen, as technical head or as head of technical work for our company, I think that there are a few points about this material that might well be brought



out since *it is a new material, relatively a new material.* [Italics supplied.]

The development of the uses of the mineral wollastonite will open up a relatively new mining industry at several locations. The industry will not at this time be limited, however, by the one deposit that we have in mind at the moment working.

[901]

\* \* \* The mineral wollastonite and its associated minerals *have no value until mined, crushed, and separated from each other*, so that the situation is a situation analogous to coal, which must be mined, crushed, and freed from slate, and delivered to a shipping point before it be of any value. [Italics supplied.]

Thus, we would request that wollastonite be valued for depletion-allowance calculations similarly to coal.

### Part III: Miscellaneous Materials (Including Industry Publications)

18-19 Mining Congress Journal (1932-33)

(October 1932 issue, page 9)

#### DEPLETION—GROSS INCOME—THE PROPERTY

By A. W. Dickinson\*

On June 6, 1932, at 5 p.m., the Revenue Act of 1932 was approved containing a provision for percentage depletion for coal and metal mines and sulphur. This provision under Section 114(b)(4) reads in part:

“The allowance for depletion shall be, in the case of coal mines, 5 percentum, in the case of metal mines, 15 percentum, and in the case of sulphur mines or deposits, 23 percentum, of the gross income from the property during the taxable year.”

\*Staff, The American Mining Congress.

It is generally understood that gross income is the amount of money received for, or the value of the marketable or shipping product of, a natural resource enterprise. The production of coal or ore, of metals or non-metals is carried on from the prospecting and discovery stages with the sole objective of developing and bringing into being a marketable shipping product of value. This value is the gross income.

The whole conduct of mining enterprise is a selective procedure. It most commonly happens that in the selection of a deposit of mineral for production many other deposits are discarded or eliminated from consideration in the desire and plan to operate only such a property as will present the best opportunity for the final winning of a marketable product. /

After the selection of the deposit of the mineral is made plans are carefully developed with a view to selecting the coal, ore or mineral to be taken from its place in the earth. Mining men do not take the entire content of the land to which they have claim or title. Coal lies in beds of varying thickness and pitch, and ores and minerals are found in veins and other forms of deposit. The material contemplated in the plan and sought in the selective process of winning to the use of mankind is the marketable material. Thus much of the content of the deposit is discarded in the very method pursued in the working or winning. In coal mining, top or bottom coal or both are frequently left in place. In many instances there is a center band or bed which is cut out and wasted in order that the coal sent to surface may be of a marketable quality. In metal mining the drifts, crosscuts and even shafts change course in the procedure of selecting the ore or mineral which will furnish a marketable product.

There is further the selection practiced in the loading of coal and ore when impurities and waste materials are cast out by hand, hand shovel and mechanical device. From the room, breast, stope, or open pit the coal or ore then proceeds to market, the selective handling continuing en route, until the evolution of mining brings out a product which has value, a product which someone will buy—a MARKETABLE SHIPPING PRODUCT. The further selection accomplished by screens, washing, smelting and refining is contiguous to, and a step in, the production of a marketable natural resource product by mining. Without each of these steps, from prospecting to the marketable product, deposits of mineral could not and would not be won and all of the practices from the prospecting drill, rock breaking coal cutting and loading down to the electrolytic vat are vital to the fruition of a mining enterprise in evolving a marketable product which can be disposed of by the taxpayer.

The individual or group conducting a mining business receives no money until disposal is made of a marketable product. This money is then used to pay for labor, powder, machinery, supplies, taxes and miscellaneous needs. The remainder of the money received for the sale of the marketable product, IF ANY, is the net; the objective of the entire venture from prospecting to disposal. In determining the "gross income from the property" from which the percentage depletion was authorized, Congress could have had in mind no other conclusion than that the money received from the sale of the marketable product was such gross income and that the Congress and its advisers so intended when Section 114(b)(4) of the Revenue Act of 1932 was written and enacted into law:

28 Mining Congress Journal (1942)

(October 1942 issue)

[48]

## WHEELS OF GOVERNMENT

As viewed by A. W. Dickinson of the American  
Mining Congress

The American Mining Congress Tax Committee is continuing negotiations with the Treasury for the purpose of arriving at a specific understanding of the meaning of the term "gross income from the property," for purposes of computing the percentage depletion allowance for mines generally and the excess profits tax exemption for strategic minerals, and of restoring [49] the interpretations and practices in effect until recently.

28 Mining Congress Journal (1942)

(November 1942 issue)

[49]

## WHEELS OF GOVERNMENT

As viewed by A. W. Dickinson of the American  
Mining Congress

[50] *"Gross income from the property"*

When Republican Senator John Thomas, of Idaho, placed percentage depletion for mines in the Revenue Act of 1932 and the Treasury Department wrote the administrative regulations, the doughty Senator and his colleagues in the Congress had the very definite idea that the ordinary ore treatment processes performed by the mine operators were to be considered as a part of the mining operation, and that the cost

thereof should not be deducted in computing the "gross income from the property." Senator Thomas knew that the Bureau of Internal Revenue has recently sought to disallow some of the treatment processes, thereby reducing the computed depletion. While the revenue bill was under debate he engaged in a discussion on the Senate floor with Finance Committee Chairman George and Senator Edwin C. Johnson, of Colorado, in the course of which he inquired whether any change was proposed in the original understanding. Senator Johnson replied that he had discussed the matter with Treasury General Counsel Randolph Paul and gave assurance that no change was contemplated in the regulations and procedures originally adopted by the Bureau of Internal Revenue and followed for many years. He stated that gravity flotation and concentration, or equivalent processes, were included in the mining operation and he said further that the furnacing of quicksilver ores, as an example, had been considered as an equivalent of gravity or flotation concentration.

This exchange of views by the Senators while the Revenue Bill of 1942 was under debate makes a clear record of the intent of Congress not to approve Treasury regulations or bureau practices which depart from the original understandings under the 1932 and 1934 acts.

292 Mining Congress Journal (Mar.-Dec. 1943)

(March 1943 issue)

[20] AMERICAN MINING CONGRESS REVIEWS ITS ACTIVITIES IN 1942

Secretary's report to members tells of broadened scope of service to meet wartime needs



[21]

*Taxes*

The work of our Tax Committee under Chairman Henry B. Fernald, in presenting the true picture of mining and its needs, has again been a most important part of the year's work. In addition to the revenue bill hearings before the Ways and Means and Finance Committees, special hearings [22] on mine taxation were held in the West by a Senate Subcommittee headed by Senator Pat McCarran of Nevada, in which our participation was requested. These developed specific information concerning the effect of taxes upon production, with particular reference to the problems of small mines, which had real value to the government and to the mining industry.

Repeated attacks upon percentage depletion were made by the Treasury in connection with the 1942 Revenue Act. At committee hearings these were answered by eight mining witnesses, from California, Idaho, Utah, Arizona, Oklahoma, Illinois, and West Virginia. A special pamphlet discussing the question in simple language was given wide circulation. By votes of 21 to 4 and 14 to 6, respectively, the Ways and Means and Finance Committees upheld existing depletion allowances, as not only justified but essential to the welfare of the mining industry and the nation. Fluorspar, ball and sagger clay, and rock asphalt were added to the minerals entitled to percentage depletion.

The intention of Congress as to the meaning of "gross income from the property," for computing percentage depletion, etc., was expressed in a floor

debate between Senator Johnson of Colorado and Senator Thomas of Idaho. The Treasury, however, is ignoring this, and insisting on deductions from gross income which seriously reduce the depletion allowance. This is of particular concern at this stage to companies producing gold and silver by the cyanide process, and to producers of certain strategic metals, notably quicksilver. Efforts to obtain a proper interpretation are being vigorously pursued.

29.2 Mining Congress Journal (Mar.-Dec. 1943)

(December 1943 issue)

[54]

#### WHEELS OF GOVERNMENT

As viewed by A. W. Dickinson of the American Mining Congress

#### *Tax Bill in Senate*

Asking that a definition of "Gross Income from the Property" be placed in the law, Donald H. McLaughlin, a member of the AMC Tax Committee, urged that this be done to confirm the intent of the Finance Committee and the Congress when percentage depletion for mines was written into the law in 1932. He urged the committee to include in the bill the amendment by Senator Edward C. Johnson of Colorado which makes it clear that mining operations are considered as including ordinary treatment processes. The amendment applies the same principles to Sections 731 and 735 of the 1942 Act which exempt strategic minerals, above-quota production and excess output from excess profits tax.

(January 1944 issue)

## [26] MINING CONGRESS ACTIVITIES IN 1943

Annual report of Julian D. Conover, secretary, at members' meeting, (December 15, 1943)

This 46th Annual Meeting of the American Mining Congress marks the close of one of the most strenuous years in nearly half a century of service to the mining industry. The problems of mining in this second year of the war have been complex, have brought more mining men than ever before into contact with the agencies of the Federal Government, have called to an increasing extent for attention and hard work on the part of your organization.

## [27]

Concerning our work in Washington I will try to be brief. I could not possibly discuss all aspects, and will merely outline some of the important matters as to which we have either taken the lead, or have co-operated with members of the industry, with members of Congress, or with officials of the Government agencies, in protecting mining's welfare. These include:

## TAX LEGISLATION

A subject constantly before us. \* \* \*

In the pending Revenue Bill, percentage depletion was spared a further direct attack through action by the Ways and Means Committee to exclude testimony on this subject. On the other hand, the House bill provides that following the war, percentage de-

pletion allowances shall be discontinued in the case of fluorspar, potash and other minerals to which this right was recently extended. We are supporting an amendment to strike out this termination clause.

Our Tax Committee, under Mr. Fernald, has met frequently. It has made exhaustive study of the effect of existing law and regulations on mining and has made careful recommendations to Congress, for consideration in the pending bill if possible, or in further legislation next year.

The committee, its subcommittees and individual members, and the staff have been active in all these matters—particularly in protecting percentage depletion provisions; in pressing for a clear-cut definition of “Gross Income from the Property” upon which the percentage depletion allowance, the strategic mineral exemption, etc., are computed—as contained in the amendment sponsored by Senator Johnson of Colorado; in presenting a similar definition of “Net Income from the Property”; \* \* \*

Mr. Fernald has again performed an outstanding service in coordinating and directing this work and in presenting the industry’s needs.

[52]

#### WHEELS OF GOVERNMENT

As viewed by A. W. Dickinson of the American Mining Congress

#### *Revenue Bill to Senate Floor*

The Thomas amendment, which would have stricken the subsection terminating percentage depletion granted to certain minerals in the present bill and in

the 1942 Act at the close of the war, was rejected; potash, however, was authorized to continue to take its percentage depletion after the war although the rate was cut from 23 percent to 15 percent.

\* \* \* \* \*

The amendment introduced by Senator Edwin C. Johnson of Colorado which places in the bill a definition of "gross income from the property" was first rejected by the Committee and then a week later on December 21 was accepted and approved. Made necessary by the recent denial by the Bureau of Internal Revenue of certain treatment costs in computing "gross income from the property" for purposes of percentage depletion, the amendment specifically defines the term "ordinary treatment processes" as including, in the case of coal—cleaning, breaking, sizing, and loading for shipment; in the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment; in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and in the case of lead, zinc, copper, gold, silver, or fluorspar ores, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, precipitation (but not including electrolytic deposition), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores.

It is provided that the Johnson amendment shall be effective as if it were a part of the Internal Revenue



Code, the Revenue Act of 1938, the Revenue Act of 1936, the Revenue Act of 1934 and the Revenue Act of 1932, on the date of its enactment.

In the Finance Committee's report, the following language is notable:

"The purpose of the provision is to make certain that the ordinary treatment [53] processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation, and to give reasonable specification of what are to be considered such processes for various kinds or classes of mines. The law has never contained such a definition, and its absence has given rise to numerous disputes. The definition here prescribed expresses the congressional intent of these provisions as first included in the law, and is in accord with the original regulations and the Bureau practices and procedures thereunder. It is, therefore, made retroactive to the date of such original provisions."

30 Mining Congress Journal (1944)

(February 1944 issue)

#### WHEELS OF GOVERNMENT

[115] As viewed by A. W. Dickinson of the American Mining Congress.

#### *Revenue bill to President*

On January 21, the Senate passed the Revenue Bill of 1943 with few changes from the form reported in our January issue. The Johnson "Gross Income From the Property" amendment was included as was also that raising the credit for exempt excess output for new coal and iron mines from  $\frac{1}{8}$  to  $\frac{1}{2}$  of the net

income, and making this provision retroactive to December 31, 1941. Potash and its crystallization process was specifically included in the definition of gross income. Through the effort of Senator McClellan (Dem., Ark.) an amendment was accepted including barite for percentage depletion at 15 percent. Last was the amendment offered by Senator Elmer Thomas (Dem., Okla.) which would have stricken the House clause terminating the percentage depletion allowance for fluorspar, ball and sagger clay, rock asphalt, flake graphite, vermiculite, beryl, feldspar, mica, talc, lepidolite, spodumene (and barite) at the end of the war; the vote on this amendment was close, 38-34.

Shortly before the passage of the bill, Finance Committee Chairman Walter George after expressing his opposition to the Thomas amendment, made some comments which the mining industry will do well to ponder deeply. He said that on the recommendation of the War Production Board a depletion allowance had been granted recently for a number of minerals but that no case had been made out for a permanent depletion rate. Senator George contrasted this action with the original placement in the law of percentage depletion for oil and gas and metals, stating that the original draft was not made in a haphazard manner but was actually done on the basis of a careful investigation and study, as the result of which it was shown that the minerals included were entitled to certain definite percentage rates. These rates, he said were authorized in place of the discovery allowance previously made in the law which had been found extremely difficult to administer.

Commenting further on the minerals recently included for the percentage depletion allowance, the Senator said "it would be a mistake to put these minerals on a permanent-percentage depletion basis

at this time without study of the competitive conditions and without demanding that sufficient data be furnished so as to enable the Congress, if it is proper hereafter to fix a permanent deduction for percentage depletion, to say what it should be. We have simply lumped them all together; they are all given 15 percent in computing their taxable income. It certainly will, I must say, upset competitive conditions and widen a gap in the Federal income tax laws as applicable to corporations that will one day, in all probability, lead to the elimination or curtailment of the percentage depletion given to oil and to other materials."

[116]

Unfortunately, the Senate amendment increasing the credit for exempt excess output of new coal and iron mines was lost but the Johnson "Gross Income from the Property" amendment is in the bill as sent to the White House, with a change made at the earnest request of the Treasury representatives who feared that the cost of smelting and refining processes might be included in the computation of gross income under the terms of the amendment. As changed, one paragraph (iv) of Section 117(c) now reads—"in the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic) cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining) or by substantially equivalent processes or combination of proc-

esses used in the preparation or extraction of the product or products from the ore, including the furnacing of quicksilver ores. The principles of this sub-paragraph shall also be applicable in determining gross income attributable to mining for the purposes of Sections 731 and 735."

The definite statement, in the bill awaiting approval, of this clear-cut definition of gross income by the Senate and House is an example of what can be accomplished by an aroused and unified mining industry, and the sincere thanks of the industry are due to Senator Edwin C. Johnson of Colorado who introduced and fought for the amendment and to Representative Wesley E. Disney of Oklahoma who exercised his rare ability in keeping it in the bill.

30 Mining Congress Journal (1944)

(November 1944 issue)

[21]

#### THE NEW IDRIA DECISION

Mining industry's contention that percentage depletion be computed on gross sales of the first marketable product upheld. Depletion also allowed on ore mined from old dumps.

By ARTHUR H. KENT,

*Attorney-at-Law,*

*San Francisco, Calif.*

The recent decision of the Circuit Court of Appeals for the Ninth Circuit in *New Idria Quicksilver Mining Company v. Commissioner* and three related cases, decided September 22, 1944, is of great interest and importance to the mining industry. Herein the Court, reversing the Tax Court of the United States which has sustained the Commissioner, held that the taxpayers, which were engaged in the mining and

treatment of cinnabar ores, were entitled to use as gross income from the property the total amount received from gross sales of flasksed quicksilver. The Commissioner had determined deficiencies based upon the deduction from such gross income of the costs of transporting and furnacing the crushed ores and the condensing, cleaning, and flasking of the quicksilver, together with an assumed profit determined by applying to total profits from quicksilver sales the percentage which the cost of each operation bore to the total cost of all operations involved.

The decision of the court on this point is of great significance in several respects. The court might have rested its decision solely upon section 124 of the Revenue Act of 1943, i.e., the gross income amendment, which added section 114(b)(4) to the Code and retroactively amended prior acts back through the Revenue Act of 1932. While that amendment in terms referred specifically, in the case of quicksilver ores, only to furnacing, the minor processes of condensing, cleaning, and flasking could reasonably be held to be included in the term "furnacing," as being merely the completion thereof and incidental thereto.

The court, however, did not confine its decision in any such fashion. Rather, it declared that it was satisfied on the basis of much consideration of the history of that amendment, that it was merely declaratory of the original intention of Congress that the processes to be excepted in arriving at the first marketable product from quicksilver ores should include the furnacing of the same. The court stated that it could find no basis for legally distinguishing the beneficiation which takes place in the rotary furnace and condensing system from the preceding processes of mining and crushing. It concluded by declaring that the interpretation of the Treasury regulation by the Commissioner



and the Tax Court was not in harmony with the statutes and the intention of the regulation prior to the amendment.

The court in this decision has recognized and adopted the principle, in the case of metalliferous ores which do not have an established or representative field price, that no gross income is realized within the meaning of the statute until the point is reached where by suitable metallurgical treatment a commercially marketable product has been obtained. This principle is equally applicable to such processes as the cyanidation and precipitation of gold and silver ores, the leaching of copper and other ores, the crystallization of potash, and similar processes. The *New Idria* decision therefore constitutes a clear judicial vindication of the interpretation of the statute and regulations which representatives of the industry since 1940 have in vain urged upon the Bureau of Internal Revenue to be the proper one. It also vindicates the contention made by Senators Edwin C. Johnson and John Thomas in the Senate that the gross income amendment conferred no new substantive benefits upon the mining industry but merely clarified the statute by declaring the original legislative intent and policy in specific and unambiguous language. Finally it represents an unmistakable judicial reverse to administrative action wearing the guise of interpretation but in reality derogatory of congressional policy and intent.

[22] Mr. Robert W. Searls of San Francisco was counsel for the taxpayers throughout this very successful litigation.

There follows the full text of the *New Idria* decision.

As viewed by A. W. Dickinson of the American  
Mining Congress

*"Gross income from the property"*

In California the U.S. Circuit of Appeals for the Ninth Circuit has reversed a decision of the U.S. Tax Court in which was involved the definition of "gross income from the property" under percentage depletion. In the case of quicksilver mining companies, the Bureau of Internal Revenue had ruled that in computing percentage depletion deduction must be made from gross income of "the cost of transporting, furnacing, condensing, cleaning, etc., in amounts agreed upon together with an assumed profit which was determined by applying to the total profits from sales of quicksilver the percentage which the cost of each operation bore to the total cost of all operations involved in getting the quicksilver to market." Robert M. Searls of San Francisco, attorney for the producers, demonstrated to the Court the lack of any market for crude cinnabar ore and asserted that furnacing of the ore is the equivalent of concentration by gravity or flotation process. In handing down its ruling the Court cited the amendment placed in the Revenue Act of 1943 by Senator Edwin S. Johnson of Colorado, which in defining "gross income from the property" specifies that furnacing of quicksilver ores is an ordinary treatment process. The Court further held that the Johnson amendment is a reaffirmation of the "intent of Congress" when percentage depletion was granted to metals in 1932.

This action of the California Court amply justifies the need for the Johnson amendment, as previously the Bureau [p. 53] had been pressing to cut down the

amount of depletion granted by deducting cost and "proportionate profits" in the case of ordinary treatment processes such as cyanidation of gold ores and the furnacing of quicksilver ores.

DEPLETION AND RELATED PROBLEMS UNDER THE REVENUE  
ACT OF 1942

By Henry B. Fernald

[21 Taxes, The Tax Magazine, 141 (1943)]

[143]

*Gross Income.*

The question of what constitutes "gross income from the property" for the purpose of allowing 15% of such gross income, and also as to what constitutes "net income from the property" has been a subject of considerable debate between taxpayers and the Bureau. This started in formulating the Treasury Regulations under the 1932 Act when many taxpayers urged that the proposed Department Regulations did not give to the law the interpretation which had manifestly been intended under the Parker-Shepherd Report of 1929 (Reports to the Joint Committee on Internal Revenue Taxation from Its Staff, Vol. I, Part 8—1929). After extended hearings on this subject before the Assistant Secretary of the Treasury, substantial modifications were made in the Bureau's original proposals and the Regulations as thus finally approved (Regulations 77, Art. 221) stood substantially unchanged until in 1940 when certain apparently minor changes therein were made in 1940 by T.D. 4960 (1940-1 C. B. 38). These changes thus made in the Regulations were in themselves appar-

ently minor in nature and effect, but a more important point is that the Bureau has from time to time, particularly since 1940, been changing its interpretations and procedures. These changes have had particular relation (a) to the point where the "cut-off" should come in computing net income for the metal mines with regard to the processes which were or which were not to be considered, in effect, as part of the mining operation, and (b) to the question of what, if any, profits should be considered as attributable to the further processes as distinguished from the mining operations.

(a) The Regulations themselves had referred to "concentrating (by gravity or flotation) and other processes to the extent which they do not benefitate the produce to a greater degree \* \* \*." The Bureau's practice under the Regulations had been for many years to consider cyaniding, leaching and certain other processes as essentially equivalent to concentrating by gravity or flotation, and it was only recently that the Bureau had been endeavoring to change its long-accepted procedures and doing this without any corresponding change in the Regulations.

(b) Under the original Regulations, for any processes beyond the concentration or equivalent processes—as for example, smelting and refining—only the costs were to be deducted in computing gross income; but the 1940 amendment to the Regulations required that there should be eliminated not merely the cost but also the "*proportionate profits attributable*" to such processes. At the time it was understood this meant the profits, if any, and that would seem to be its natural meaning. Quite recently, the Bureau has proposed determinations to make an allocation of the entire profits of a mining enterprise ratably on the basis of the relative costs below and beyond the cut-off point.

### *Details To Be Handled by Regulations.*

Manifestly, this raised the question of whether the Bureau was justified in changing the long-established regulations and procedures without any corresponding change in the law and also the question of whether the re-enactment of the law without change served to confirm and approve any departmental rulings or Bureau interpretations which were in effect at the time of re-enactment of the law. There was particular question regarding this in connection with the present Act. It was suggested that to avoid question, a provision should be written into the law as to what was meant by gross and net income from the property and what was meant by income from mining in certain other sections of the law. The Treasury urged that the law should not attempt to deal with such details but that they should be left to be handled under Treasury regulations. There was, of course, recognition that there must be some limit to the amount of detail to be written into the law, but at the same time it was not contemplated that Congress' intent with respect to the law and its application should be considered as changed simply because the law was re-enacted at a time when someone within the Bureau was proposing to make radical changes in the application of prior provisions. This gave rise to a discussion on the floor of the Senate between Senator Thomas and Senator Johnson (Congressional Record, October 19, 1942, p. 8291) in which it is stated that [172] there is no intention in the present law to make any change from the original intent, and Mr. Paul is quoted as having stated the Treasury's intention to adhere to the original regulations and procedures, excepting only "that there would be excluded from gross income from the property not only the cost of further processes such as smelting, but also



the profits, if any, attributable thereto; intending thus to make the charges for a mining company's own smelter compare with those of an independent customs smelter." I suggest that those of you particularly interested in this question read this discussion. Without trying to pass upon its legal effect, I think it makes clear the intention of Congress in this regard.

BRICK AND CLAY RECORD

[Cover Page:]

BRICK—REFRACTORIES—STRUCTURAL TILE—SEWER  
PIPE—DRAIN TILE

BRICK AND CLAY RECORD

Vol. 119, No. 5—November, 1951

(Leading clay journal of the world)

[24] CLAY DEPLETION ALLOWANCES GRANTED IN NEW  
TAX BILL

The President on Oct. 20 signed H.R. 4473, the Revenue Act of 1951 which increases individual income taxes and corporate taxes. A provision of this bill granted 5 percent depletion allowances to brick and tile clay and 15 percent depletion allowances on refractory and fire clay.

Text of Section 319 of the Revenue Act of 1951, dealing with depletion percentages, follows:

*The depletion allowances apply to the market value of the raw minerals and cannot exceed 50 percent of the net profits from the property. [Italics supplied.]*

[25] TAKE DEPLETION ALLOWANCE AFTER CAREFUL  
STUDY

A full calendar year has now elapsed since the effective date (Dec. 31, 1950) of the depletion section of the Revenue Act of 1951. Manufacturers will claim the new percentage depletion on their Federal Income Tax returns for the full year just ended.

The interpretation of where a "commercially marketable product" obtains has still to be definitely established, however, and presents a knotty problem to the clay products and refractories manufacturer.

Current thinking in the structural clay products industry reflects the opinion that the "ordinary treatment" required to obtain a marketable product includes the normal processes of screening, tempering, forming, drying and firing. Most structural clay products firms, therefore, are expected to base their depletion on the gross income from the final burned product.

*Due to the fact that there is an established market and regular commerce in fire clay, quartzite, and similar refractory raw materials, the situation in that industry is considerably different. In this case, legal opinion tends to consider that a "commercially marketable product" is produced when the mined material is in a size suitable for shipment. Even those refractory producers who do not normally buy or sell such raw material will probably be required to establish a price for the self-mined materials; such a price to be based on the average market prices of such materials in his particular area. [Italics supplied.]*

In the case of the refractory producer in particular,

however, individual analysis by qualified tax advisors must be the watchword. BRICK AND CLAY RECORD has been advised by a tax consultant to strongly urge each refractory firm to obtain qualified, individual tax guidance, since the problem and its solution will be subject to variation in each case.

[29] NEWS OF THE INDUSTRY

SCPI Committee Issues  
Depletion Interpretation

A Structural Clay Products Institute Committee consisting of Edwin H. Davis, Norman H. Crissey, and Kenneth W. Dunwoody has issued its interpretation of the new depletion allowance in the form of a memo to the members of the industry. It has requested comments on its interpretation.

Here is the memo in part:

"Section 114(b)(4)A of the Internal Revenue Code as amended provides, that:

A. In General—the allowance for depletion under Section 23(m) in the case of the following mines and other natural deposits shall be—

1. In the case of \* \* \* brick and tile clay \* \* \* 5 per centum \* \* \* of the gross income from the property.

B. Definition of Gross Income From Property.—As used in this paragraph the term 'gross income from the property' means the gross income from mining. The term 'mining' as used herein, shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the

ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plant or mills \* \* \*."

This section defines "**ordinary** treatment processes" in the case of coal, sulphur, iron ore, bauxite, ball and sagger clay, rock asphalt and other minerals. We have no such definitions for treatment processes of brick and tile clay under subparagraph "B" and must therefore interpret the statute from the language used by the Congress.

The word "mineral" in its ordinary and common meaning, generally includes stone and rock deposits, whether obtained from a mine, as the word would seem to imply, or by open Working, and whether containing metallic substances or substances entirely non-metallic. (58 CJS p. 24)

Unless there are words qualifying or limiting its meaning the term "mineral" as used in instruments and statutes ordinarily includes asphaltum, chrome or chromate of iron, **clay**, coprolites, diamonds, granite, marble, salt, shale and silica \* \* \*.

\* \* \* Treasury Regulations 111, \* \* \* includes "clay" within the definition of minerals.

The statute provides that the term "mining" shall include not merely the extraction of the clay (minerals) from the ground, but also the **ordinary** treatment processes normally applied by mine owners in order to obtain the commercially marketable mineral product or products.

The word "ordinary" is defined in Webster's New International Dictionary to mean "customary, usual, regular." \* \* \*

*It is the normal, customary and necessary practice for manufacturers of clay products to burn their pro-*

ductions in order to obtain the commercially marketable product. Raw brick and tile clay does not have a commercially marketable value \* \* \*.

\* \* \* Under the language of the statute depletion must be based on the value of the burned product \* \* \*.

\* \* \* For the above reasons, a brick and tile manufacturer has no "commercially marketable product" until the green brick formed of raw brick or tile clay has been burned. The depletion allowance should be based on the gross income from burned brick or tile including the loading for shipment which is the first point at which clay becomes marketable. [Italics supplied.]

Senate Hearings, 1938

(Revenue Act of 1938, Hearings before the Committee on Finance, United States Senate, 75th Cong., 3d Sess., on H.R. 9682)

[484] Statement of D. A. CALLAHAN, of Wallace, Idaho, representing the American Mining Congress.

Mr. CALLAHAN: Mr. Chairman, I am representing the American Mining Congress and I have here a brief which I will not read, but I just want a few minutes to tell you orally what this is all about.

The CHAIRMAN. Very well.

(The brief referred to is as follows:)

Statement of D. A. CALLAHAN, Wallace, Idaho, on the Revenue Bill of 1938, presented at Hearings of the Committee on Finance, United States Senate, March 19, 1938.

To the honorable Committee on Finance, United States Senate:

I am appearing here in behalf of the American Mining Congress to urge an amendment to section 22(c) of the bill. In doing so I am representing the entire industry from the producer to the fabricator of metal products.



This provision, which is a repetition of the present law, confers upon the Commissioner of Internal Revenue the authority of prescribing the basis of inventories which will clearly determine the income of a taxpayer. Under this law the Treasury Department refuses to permit those engaged in the metal smelting, refining, and fabricating industries to apply current costs to current sales in determining the cost of goods sold. The American Mining Congress urges that this section be amended to permit these industries to use this method.

\* \* \* \* \*

In order to arrive at an understanding of just what this means, I shall outline the processes through which raw metal must pass before reaching the market as a finished and merchantable product.

First the ore is taken from the ground, is crushed and ground, and the waste material separated usually through what is known as the flotation process. This reduces the metal to the form known as concentrates.

Next the concentrates are shipped to the smelter where they go through several processes before emerging as a merchantable product. Certain of the metals must go through processes of refining in order to remove all impurities.

Metallurgical improvements over the past several years have resulted in the final production of a practically pure form of metal. These processes consume a considerable period of time and during this period the smelter and refiner must carry large inventories because the smelting and refining business is a continuous process and must not be impeded or delayed by lack of metal in the form of concentrates, and the smelting and refining company must carry stocks of refined metal to meet the demands of the market.

In these various steps from the mine to the market of the finished product, there is a community of interest between the producer of the raw materials, the smelter, the refiner, and the fabricator. In a great many cases the producing company makes a contract with a smelting company under the terms of which settlements are made upon the basis of the market price on the day the concentrates are shipped to, or received by, the smelter. This contract provides, among things, for a smelting charge or toll, and in many cases, the smelter acts in effect as the selling agent for the finished product. This is necessary because small producers cannot maintain the selling organization and have not the means which will enable them to wait for returns until the finished product is finally sold to the fabricator. By sampling and assay the exact refined metal content of the concentrates is determined at the time of delivery and the producer is then paid the market price, for the refined metal equivalent of his product, less a specified charge for smelting and refining. At that point the producer's responsibility in respect to that production is terminated and that of the smelter and refiner begins.

Basically, smelting and refining is a custom business and a substantial part of present-day operations are conducted on a direct toll basis. Obviously, however, the small producer of crude ores is not financially able to carry the metals through the smelting and refining period. Accordingly, a substantial part of the business [485] must be conducted on what is known as the ore purchase contract basis which I have described.

Experience has taught the custom smelter and refiner that he cannot afford to speculate on metal price fluctuations. The risk of loss is too great, the processing period is too long, metal prices are subject to extreme and rapid fluctuations. A large part of the price of the refined metals represents the cost of the

crude ores. There is no adequate metal futures market for hedging.

Accordingly, the custom smelter and refiner protects himself by selling the metals produced from the crude ores which have been purchased at the price paid for them. In the absence of a metal futures market there is only one method available for obtaining this result and that method is employed in the industry to the fullest practical limit. It consists of selling, concurrently with the purchase of crude ores, an amount of refined metal equivalent to the metal content of the ore purchased. The price paid for the metals in the ores is thereby matched with the price received for the refined metals. The effect of subsequent fluctuations in metal prices is neutralized, the smelting and refining fee charged the producer is protected, and the profits from operations on the purchase contract basis coincide with those derived from toll operations. This, of course, cannot be carried out with absolute mathematical exactness, but it is the basic buying and selling policy of the industry, and in ordinary times it can be and is carried out with remarkable accuracy. This accuracy results from two factors: (1) Close co-operation between the receiving and selling departments, and (2) the ability to determine the exact refined metal content of the crude ore or concentrates. This second factor is essential to a matching policy and distinguishes the metal-process industries from the ordinary manufacturers who do not and cannot employ it.

Notwithstanding the fact that the custom smelter and refiner conducts his business so as to eliminate the risks of market fluctuations, he is obliged under the present rules of the Internal Revenue Bureau to reflect such fluctuations in the computation of his taxable net income. This result is produced, because he is not permitted to apply the cost of current purchases

against current sales, which conforms to the basis of conducting his business, but is obliged to apply the so-called first-in, first-out rule in determining the cost of goods sold. This latter rule assumes that the raw materials purchased first are used first; and correspondingly, that those purchased last are used last.

This rule cannot fairly be applied to the smelting and refining industry, because in order to operate efficiently the custom smelter and refiner must maintain a substantial amount of stocks on hand. These stocks include: (a) The metal impounded in the system necessary to permit continuous smelting and refining operations, (b) sufficient metals on hand to assure compliance with toll contract commitments, and (c) an adequate supply of metals to carry out the policy of currently selling against intake. The first-in, first-out rule goes back through the entire inventory, picks up the cost of the earliest purchase, and applies it to the present sale. As a result, the entire net fluctuations in market price since the date of the earliest purchase, which was probably several months before, is reflected as profit or loss on each sale of refined metals—although from the business point of view, the sale is made for the very purpose of eliminating the effect of such fluctuations. This introduces a speculative element into the computation of the taxable income which is wholly absent in the conduct of the business.

The method of matching current sales against current purchases has desirable results for both the producer and the processor. It assures the processor of his operating profit or toll and enables him to pay the producer upon delivery of his metal to the smelter. It also assures the producer of a market free from the speculative element which would result if the smelter purchased his metals and held them for future sales. So long as this practice is followed, the method

of accounting employed by the smelter and refiner should conform thereto and taxable net income should be based upon such method.

TRADE DEFINITIONS OF THE VARIOUS "ORDINARY TREATMENT PROCESSES" LISTED IN CODE SECTION 114(b) (4)(B) AND OF THE SPECIFICALLY EXCLUDED PROCESSES

*Processes included in "ordinary treatment processes":*

**Sulphur processes:** The processes listed for sulphur, "pumping to vats, cooling, breaking, and loading for shipment" are the processes used in connection with the "Frasch process," under which the sulphur is first liquefied in place by pumping hot water under pressure into drill holes and is then pumped to the surface to vats where it is cooled in a big block and later broken and loaded by power shovels into railroad cars.<sup>1</sup>

**Coal processes:** The processes listed for coal are "cleaning" (for the purposes of separating out impurities, which may be done by a number of different physical or mechanical processes); "breaking," to reduce the size of the material to put it in shipping form, to make the material more suitable for direct marketing, to free impurities for further removal of impurities, or for all three purposes; "sizing," a process of separating mixed sizes, usually by screening; and loading for shipment.<sup>2</sup>

<sup>1</sup> See Mineral Facts and Problems, Bulletin 556, Bureau of Mines (1956), p. 848; House Hearings, 1932 (*supra*, pp. 438-439); House Hearings, 1951, *supra*, pp. 440-441.

<sup>2</sup> Mitchell, Coal Preparation, Seeley W. Mudd Series (A.I.M.E., 1950 ed.), pp. 182, 188, 190, 191, 246; Taggart, Handbook of Ore Dressing (1927 ed.), pp. 56, 498; Taggart, Elements of Ore Dressing (1931 ed.), p. 17; Gaudin, Principles of Mineral Dressing (1939 ed.), p. 14; Richards and Locke, Textbook of Ore Dressing (1940 ed.), pp. 104, 497-498, 503, 508, 516.



Other processes included as "ordinary treatment processes"

"*beneficiation*": This means the enrichment of a material by separating out the worthless from the valuable components without significantly altering the inherent physical and chemical nature of either.<sup>3</sup> In relation to ores, it means preparing the ore for the smelter (by concentration (see *infra*) or otherwise).<sup>4</sup> Thus, in some instances "beneficiation" has a slightly broader meaning than "concentration."

"*concentration*": This is any process (and there are numerous ones) which separates the valuable constituent (or mineral) from the valueless, or which separates one valuable mineral from another valuable mineral, by essentially physical means.<sup>5</sup> With only slightly different connotations, the following terms are synonymous with concentration: "mineral dressing," "ore dressing," "beneficiation," and "milling."<sup>6</sup>

#### *Types of concentration:*

"*gravity*": The separation of the valuable mineral from the valueless constituent by gravity is a process dependent upon the difference in the specific gravity or density of the mineral and valueless constituent.<sup>7</sup> Coal washing, for instance, depends upon gravity-concentration principles.<sup>8</sup>

<sup>3</sup> Materials Survey—Copper, U.S. Bureau of Mines with Cooperation of Geological Survey, Department of the Interior (Sept. 1952), Ch. II, p. 26; Werner, *Materials Beneficiation Enters New Fields*, Battelle Technical Review (Sept. 1959), vol. 8, No. 9, p. 4.

<sup>4</sup> Webster's New International Dictionary (1947 ed.)

<sup>5</sup> Taggart, *Handbook of Ore Dressing* (1927 ed.), p. 3; Richard and Locke, *Textbook of Ore Dressing* (1940 ed.), p. 5.

<sup>6</sup> Materials Survey—Copper, *supra*, Ch. II, p. 26.

<sup>7</sup> Taggart, *Elements of Ore Dressing* (1951 ed.), 105 and 165.

<sup>8</sup> Mitchel, *Coal Preparation*, *supra*, p. 246; Richards and Locke, *Textbook of Ore Dressing* (1940 ed.), p. 498.

**"flotation"**: A concentration process which, through the use of chemicals used in water applied to a mixture of finely ground minerals, causes a selective attachment of gas bubbles to one mineral constituent and results in a change of effective specific gravity of that mineral, thus permitting a gravitational separation of components. No significant chemical change is involved.<sup>9</sup>

**"amalgamation"**: A concentration process by which native metals (gold and silver) are separated from nonmetallic worthless minerals as a result of the fact that gold and silver have a greater affinity for mercury while the worthless material has a greater affinity for water. The resulting product (impure gold or silver) is the product which is sent to the smelter or refiner.<sup>10</sup>

**"electrostatic"**: A concentration process under which minerals of different electrical conductivity are separated from each other.<sup>11</sup>

**"magnetic"**: A concentration process whereby some minerals are separated out of a material through electromagnetic attraction.<sup>12</sup>

**"crushing"**: Is an operation or group of operations whereby large lumps are reduced in size. Generally, the minimum size is approximately  $\frac{1}{20}$  or  $\frac{1}{4}$  of an inch. (The cited authorities disagree on this). This

<sup>9</sup> Taggart, Elements of Ore Dressing (1951 ed.), p. 246; Taggart, Handbook of Mineral Dressing (1945 ed.), p. 12-01; Werner, Minerals Beneficiation Enters New Fields, Battelle Technical Review (Sept. 1959), vol. 8, No. 9, p. 4.

<sup>10</sup> Taggart, Elements of Ore Dressing (1951 ed.), p. 334; Taggart, Handbook of Mineral Dressing (1945 ed.), p. 14-10; Gaudin, Principles of Mineral Dressing (1939 ed.), p. 473.

<sup>11</sup> Gaudin, Principles of Mineral Dressing (1939 ed.), p. 465; Taggart, Elements of Ore Dressing (1951 ed.), p. 61.

<sup>12</sup> Richard and Locke, Textbook of Ore Dressing (1940 ed.), p. 4; Taggart, Elements of Ore Dressing (1951 ed.), p. 44.

process is used (1) to meet commercial product requirements, (2) for liberation of the mineral components in order to facilitate concentration (separating out the valuable from the valueless components), and (3) a step toward further reduction in size.<sup>13</sup>

**"crystallization"**: A process of solidifying from a liquid into a crystalline form.<sup>14</sup>

**"cyanidation"**: This applies only to gold and silver and employs a dilute solution of sodium or potassium cyanide to dissolve the metals, after which the metal solution is separated from the undissolved valueless constituent through filtration.<sup>15</sup>

**"furnacing of quicksilver"**: A distillation process by which the cinnabar ore of mercury is heated to volatilize the mercury and is followed by condensation of the mercury vapor. This may be done even by a prospector, through use of a small retort.<sup>16</sup>

**"grinding"**: This is distinguishable from crushing only in that it is a later stage in size reduction which produces an extremely fine (or pulverized) material.<sup>17</sup>

<sup>13</sup> Richards and Locke, *Textbook of Ore Dressing* (1940 ed.), pp. 5 and 19; Gaudin, *Principles of Mineral Dressing* (1939 ed.), p. 70; Taggart, *Elements of Ore Dressing* (1951 ed.), p. 341; Taggart, *Handbook of Mineral Dressing* (1945 ed.), p. 4-01.

<sup>14</sup> Taggart, *Handbook of Mineral Dressing* (1945 ed.), p. 14-24; Peele, *Mining Engineers' Handbook* (1952 ed.), p. 10-398; *Mineral Facts and Problems*, Bulletin 556, *supra*, pp. 707, 757.

<sup>15</sup> *Mineral Facts and Problems*, Bulletin 556, *supra*, p. 313; Stoughton and Butts, *Engineering Metallurgy* (1926 ed.), pp. 347, 348; Peele, *Mining Engineers' Handbook* (1945 ed.), vol. II, pp. 33-09 through 33-25.

<sup>16</sup> *Materials Survey—Mercury*, U.S. Bureau of Mines I.C. 7941, pp. 34 and 41.

<sup>17</sup> Gaudin, *Principles of Mineral Dressing* (1939 ed.), p. 92; Taggart, *Elements of Ore Dressing* (1951 ed.), p. 388.

**"leaching"**: A process of dissolving metals out of ore by means of a weak chemical solution.<sup>18</sup>

**"precipitation"**: This follows cyanidation and leaching. As applied to cyanidation, it is the process of adding, to the cyanide solution containing gold and/or silver, zinc or another metal which is chemically more active than gold or silver and which results in an ejection of impure gold and/or silver in solid form. In the case of leaching, precipitation (other than electrolytic deposition) is the process of adding, to the leach solution of a metal such as copper, iron or another metal which is chemically more active than the solution metal, and which results in an ejection of the desired impure metal in solid form.<sup>19</sup>

**"sintering"**: A process under which ore is subjected to a high temperature so that fine particles are formed into a porous, clinker-like mass.<sup>20</sup>

**"sorting"**: Hand-picking to separate out the better pieces of broken material; is a crude method of concentration.<sup>21</sup>

<sup>18</sup> Materials Survey—Copper, *supra*, Ch. II, p. 57; Stoughton and Butts, *Engineering Metallurgy* (1926 ed.), p. 99; Behre and Arbiter, *Distinctive Features of the Mineral Industries, Economics of the Mineral Industries* (A.I.M.E., 1959 ed.), p. 69.

<sup>19</sup> Materials Survey—Copper, *supra*, Ch. II, pp. 57-58; Henderson and Bates, *Metallurgical Dictionary* (1953); Stoughton and Butts, *Engineering Metallurgy* (1926 ed.), pp. 103, 301 and 348; Peele, *Mining Engineers' Handbook* (1945 ed.), vol. II, pp. 33-08 and 33-10.

<sup>20</sup> Materials Survey—Iron Ore, U.S. Bureau of Mines with Cooperation of Geological Survey, Department of the Interior (May 1956), Ch. III, p. 13; Roe, *Iron Ore Beneficiation* (1957 ed.), p. 246.

<sup>21</sup> Taggart, *Elements of Ore Dressing* (1951 ed.), p. 11; Richards and Locke, *Textbook of Ore Dressing* (1940 ed.), pp. 100-103; Peele, *Mining Engineers' Handbook* (1945 ed.), vol. II, Ch. 28, p. 15.

*Processes excluded from "ordinary treatment processes":*

*"electrolytic deposition"*: A process used in refining a metal, such as copper, by passing electric current through a metal compound solution. The pure metal is deposited on the cathode while the impurities collect as a slime at the bottom of the cell or dissolve in the electrolyte.<sup>22</sup>

*"smelting"*: The process of melting an ore accompanied by a chemical change so that the molten products are different from the substance existing before the conversion to a liquid form. In "thermal" smelting, a fuel is the source of heat.<sup>23</sup> In "electric" smelting the heat is derived from electrical energy.<sup>24</sup>

*"refining"*: The process of removal of impurities from impure metal (the product of the smelter or leaching plant) by (1) heat induced chemical reactions between constituents in molten crude metal, frequently induced or accelerated by the addition of deoxidizers, scavengers and other additives, or (2) by electrolytic methods.<sup>25</sup>

*"roasting"*: Any heating operation for the purpose of driving off volatile matter or to effect certain chemical changes at temperatures below those required for complete fusion.<sup>26</sup>

<sup>22</sup> Webster's New International Dictionary (1947 ed.); Henderson and Bates, Metallurgical Dictionary (1953 ed.); Stoughton and Butts, Engineering Metallurgy (1926 ed.), p. 95.

<sup>23</sup> Webster's International Dictionary (1947 ed.); Stoughton and Butts, Engineering Metallurgy (1926 ed.), pp. 74 and 87.

<sup>24</sup> Stoughton and Butts, Engineering Metallurgy (1926 ed.), p. 110; Newton, Introductions to Metallurgy (1948 ed.), p. 603.

<sup>25</sup> Stoughton and Butts, Engineering Metallurgy (1926 ed.), pp. 93-94; Webster's New International Dictionary (1947 ed.); Henderson and Bates, Metallurgical Dictionary (1953).

<sup>26</sup> Henderson and Bates, Metallurgical Dictionary (1953 ed.); Stoughton and Butts, Engineering Metallurgy (1926 ed.), p. 79.



# CHART OF PRODUCTS IN RELATION TO WHICH VARIOUS BRANCHES OF MINING INDUSTRY SOUGHT PERCENTAGE DEPLETION

Year percentage depletion was first granted	Product on which percentage depletion was sought or sponsored before Congress					Legislative references
	Depletable deposit	General description of form in which found	Processes applied, according to industry, representatives or sponsors	Product which results from stated processes or was specifically stated to be the marketable product		
1932	Coal	Solid	Erasmith method process	Coal		Senate Hearings, 1951, pp. 1409-1415 (App. B, pp. 342-348); House Hearings, 1952, pp. 339-341 (App. B, pp. 438-440); House 1951, p. 1607 (App. B, pp. 440-441)
	Sulphur	Pure solid		Sulphur		
	Metal mines:					
	Iron ore	Ore	Concentration for low-grade ore preparation for smelter	Shipping grade iron ore		Senate Hearings, 1942, p. 985 (App. B, pp. 360-361); Senate Hearings, 1951, p. 301 (App. B, pp. 362-363)
	Copper	"	"	Concentrates		See our main brief, Point II B 3
	Gold	"	"	"		"
	Lead	"	"	"		"
	Silver	"	"	"		"
	Zinc	"	"	"		"
1942	Ball clay	Clay	None stated	Ball clay		Senate Debate, 1942, pp. 8021, 8023 (App. B, pp. 327-328); House 1947, pp. 63, 65, 66 (App. B, pp. 328-330); Senate Hearings, 1951, (App. B, pp. 330-331)
	Fluorspar	Rock or ore	Processes somewhat similar to those employed for metallic ores	Fluorspar (ground)		Senate Debate, 1942, p. 8024 (App. B, pp. 349-351); House Hearings, 1947, p. 19 (App. B, pp. 351-352)
	Rock asphalt	Oil-impregnated rock	Crushing or grinding	Rock asphalt (crushed or ground)		Senate Hearings, 1942, pp. 1406, 1410-1412 (App. B, pp. 407-408); Senate Debate, 1942, p. 8023 (App. B, pp. 410-411); House Hearing, 1947, (App. B, pp. 411-413)
1943	Barite	Barite bearing clay	Concentration by washing and gravitation	Barite (crushed and ground)		Senate Hearings, 1943, p. 968 (App. B, p. 318); House Hearing, 1951, (App. B, pp. 318-320)
	Potash	(1) Solid	Separation from sodium chloride	Potash		House Hearings, 1950, pp. 386-387, 2231 (App. B, pp. 402-405); House Hearings, 1951, pp. 1621, 1626 (App. B, p. 406)
		(2) In brine	Evaporization, crystallization	Potash		Senate Hearings, 1943, p. 369 (App. B, pp. 401-402)
	Talc		Crushing, grinding	Talc (ground)		House Hearings, 1947, pp. 26, 37 (App. B, pp. 441-442); House Hearings, 1951, pp. 432, 434, 491, 2892 (App. B, pp. 442-446); Senate Hearings, 1951, (App. B, p. 446); House Hearings, 1951, pp. 1585-1586 (App. B, pp. 446-447); House Hearings, 1953, pp. 2035-2037, 2041-2042 (App. B, pp. 447-448)
	Vermiculite		Screening and drying and/or air separation	Vermiculite concentrate		Senate Hearings, 1943, pp. 843-844 (App. B, pp. 455-456); House Hearings, 1947, pp. 43-44, 53 (App. B, pp. 456-460); House Hearings, 1951, pp. 415, 416 (App. B, pp. 460-462); House Hearings, 1951, pp. 1612, 1613 (App. B, pp. 462-463)
1947	Bentonite	Clay	Drying, grinding or granulating	Bentonite (crude and ground)		House Hearing, 1947, pp. 66-69 (App. B, pp. 320-322); Senate Hearings, 1951, pp. 447-450 (App. B, pp. 322-325)
	China (or kaolin) clay	Clay	None stated	China clay, f.o.b. mine		House Hearings, 1950, p. 329 (App. B, pp. 334-335)
	Phosphate rock	Rock	Sintering or nodulizing for low-grade rock	Phosphate rock		House Hearings, 1950, p. 382 (App. B, p. 397); House Hearings, 1951, pp. 1637-1638 (App. B, p. 398); Senate Hearings, 1954, pp. 1335, 1336 (App. B, pp. 399-401)
	Thenardite (or salt cake)	(1) Solid	None stated	Thenardite		House Hearings, 1947, pp. 29-30 (App. B, pp. 451-452); House Hearings, 1951, pp. 2894-2895 (App. B, pp. 453-454)
		(2) In brine	Separating, sometimes by evaporation	"		
1951	Trona			Trona		House Debate, 1947, p. 9629 (App. B, pp. 454-455)
	Asbestos			Asbestos fibers as a raw material		Senate Hearings, 1951, pp. 866-868 (App. B, pp. 316-318)
	Borax	(1) Solid	None stated	Crude, white soluble powder		House Hearings, 1950, pp. 2887, 2890 (App. B, pp. 325-326); Senate Hearings, 1951, p. 1060 (App. B, p. 326)
		(2) In brine		"		
	Dolomite	Stone		Crushed stone		Same citations as for "limestone, ordinary," <i>infra</i>
	Fire and refractory clay	Clay	None stated	Clay as a raw material used in manufacturing refractory products		House Hearings, 1950, pp. 449-450, 455-463 (App. B, pp. 336-340)
	Fuller's earth	Clay	None stated	Fuller's earth		House Hearings, 1951, pp. 1618-1619 (App. B, pp. 352-353)
	Garnet		None stated	Garnet		Senate Debate, 1951, p. 12218 (App. B, p. 354)
	Granite			(1) Crushed stone		Same citations as for "limestone, ordinary"; also, House Hearings, 1951, p. 2890 (App. B, pp. 356-357); Senate Hearings, 1951, p. 1061 (App. B, p. 357); Senate Hearings, 1954, p. 1213 (App. B, p. 358)
			Asked for but was not granted advanced processing	(2) Dimension stone		Senate Hearings, 1954, pp. 1213-1215 (App. B, pp. 358-360)
	Limestone, ordinary (calcium carbonates)	Stone		Crushed stone		House Hearings, 1950, pp. 480-483, 487-490 (App. B, pp. 363-366); House Hearings, 1950, pp. 808-809, 811 (App. B, pp. 370-372); House Hearings, 1951, pp. 1631-1636 (App. B, pp. 373-376); Senate Hearings, 1951, pp. 891-895 (App. B, pp. 376-379); House Hearings, 1953, p. 2101 (App. B, pp. 379-381)
	Limestone, chemical grade	Stone		Crushed stone		Same citations as for "limestone, ordinary," plus House Hearings, 1951, pp. 332-340 (App. B, pp. 381-386); House Hearings, 1951, pp. 1566-1569 (App. B, pp. 387-390); Senate Hearings, 1951, pp. 1566-1569 (App. B, pp. 387-390); House Hearings, 1953, pp. 2091-2092 (App. B, pp. 392-394)
	Limestone, metallurgical grade	Stone		Crushed stone		Same citations as for "limestone, ordinary" and for "limestone, chemical grade," plus House Hearings, 1953, pp. 2059-2060 (App. B, pp. 394-395)
	Magnesite	Rock	Crushing, concentration, burning	Dead-burned magnesite		Same citations as for "limestone, ordinary"
	Marble	Stone		Crushed stone		Same citations as for "limestone, ordinary"
	Quartzite		None stated	Quartzite as a raw material used in manufacturing refractory products		Same citations as for fire clay
				Sand and gravel		House Hearings, 1950, p. 310 (App. B, pp. 413-414); Senate Hearings, 1951, p. 1061 (App. B, p. 414)

	Fluorspar	Rock or ore	Processes somewhat similar to those employed for metallic ores	Fluorspar (ground)	(App. B, pp. 330-331)
	Rock asphalt	Oil-impregnated rock	Crushing or grinding	Rock asphalt (crushed or ground)	Senate Debate, 1942, p. 8024 (App. B, pp. 349-351); p. 19 (App. B, pp. 351-352)
1943	Barite	Barite bearing clay	Concentration by washing and gravitation	Barite (crushed and ground)	Senate Hearings, 1942, pp. 1400, 1410-1412 (App. B, Debate, 1942, p. 8023 (App. B, pp. 410-411); House H. (App. B, pp. 411-413)
	Potash	(1) Solid	Separation from sodium chloride	Potash	Senate Hearings, 1943, p. 968 (App. B, p. 318); House (App. B, pp. 318-320)
	Talc	(2) In brine	Evaporization, crystallization	Potash	House Hearings, 1950, pp. 386-387, 2231 (App. B, pp. 4 inga, 1951, pp. 1621, 1626 (App. B, p. 406)
			Crushing, grinding	Talc (ground)	Senate Hearings, 1943, p. 369 (App. B, pp. 401-402)
	Vermiculite	—	Screening and drying and/or air separation	Vermiculite concentrate	House Hearings, 1947, pp. 26, 37 (App. B, pp. 441-442); pp. 432, 434, 491, 2892 (App. B, pp. 442-446); Senate (App. B, p. 446); House Hearings, 1951, pp. 1585-1586
1947	Bentonite	Clay	Drying, grinding or granulating	Bentonite (crude and ground)	House Hearings, 1953, pp. 2035-2037, 2041-2042 (App. Senate Hearings, 1943, pp. 843-844 (App. B, pp. 455-1947, pp. 43-44, 53 (App. B, pp. 456-460); House H. 415, 416 (App. B, pp. 460-462); House Hearings, 1951 B, pp. 462-463)
	China (or kaolin) clay	Clay	None stated	China clay (f.o.b. mine)	House Hearing, 1947, pp. 66-69 (App. B, pp. 320-322); pp. 447-450 (App. B, pp. 322-325)
	Phosphate rock	Rock	Sintering or nodulizing for low-grade rock	Phosphate rock	House Hearings, 1950, p. 329 (App. B, pp. 334-335)
	Thenardite (or salt cake)	(1) Solid	None stated	Thenardite	House Hearings, 1950, p. 382 (App. B, p. 397); House 1637-1638 (App. B, p. 398); Senate Hearings, 1954, p. pp. 399-401)
		(2) In brine	Separating, sometimes by evaporation	"	House Hearings, 1947, pp. 29-30 (App. B, pp. 451-452); pp. 2894-2895 (App. B, pp. 453-454)
1951	Trona	—	—	Trona	House Debate, 1947, p. 9629 (App. B, pp. 454-455)
	Asbestos	(1) Solid	None stated	Asbestos fibers as a raw material	Senate Hearings, 1951, pp. 866-868 (App. B, pp. 316-31
	Borax	(2) In brine	—	Crude, white soluble powder	House Hearings, 1950, pp. 2887, 2890 (App. B, pp. 325-1951, p. 1060 (App. B, p. 326)
	Dolomite	Stone	—	Crushed stone	Same citations as for "limestone, ordinary", <i>infra</i>
	Fire and refractory clay	Clay	None stated	Clay as a raw material used in manufacturing refractory products	House Hearings, 1950, pp. 449-450, 455-463 (App. B, p.
	Fuller's earth	Clay	None stated	Fuller's earth	House Hearings, 1951, pp. 1618-1619 (App. B, pp. 352
	Garnet	—	None stated	Garnet	Senate Debate, 1951, p. 12218 (App. B, p. 354)
	Granite	—	—	(1) Crushed stone	Same citations as for "limestone, ordinary"; also, 1 p. 2890 (App. B, pp. 356-357); Senate Hearings, 1 p. 357); Senate Hearings, 1954, p. 1213 (App. B, p.
	Limestone, ordinary (calcium carbonates)	Stone	Asked for but was not granted advanced processing	(2) Dimension stone	Senate Hearings, 1951, pp. 1213-1215 (App. B, pp. 358
			—	Crushed stone	House Hearings, 1950, pp. 480-483, 487-490 (App. B. Hearings, 1950, pp. 808-809, 811 (App. B, pp. 370-1951, pp. 1631-1636 (App. B, pp. 373-376); Senat 891-895 (App. B, pp. 376-379); House Hearings, 1 pp. 379-381)
	Limestone, chemical grade	Stone	—	Crushed stone	Same citations as for "limestone, ordinary," plus H pp. 332-340 (App. B, pp. 381-386); House Hearings, 1566-1569 (App. B, pp. 387-390); Senate Hearings, 1 (App. B, pp. 390-392); House Hearings, 1953, p. pp. 392-394)
	Limestone, metallurgical grade	Stone	—	Crushed stone	Same citations as for "limestone, ordinary" and for "lim
	Magnesite	Rock	Crushing, concentration, burning	Crushed stone	House Hearings, 1953, pp. 2059-2060 (App. B, pp. 394
	Marble	Stone	—	Dead-burned magnesite	Same citations as for "limestone, ordinary"
	Quartzite	—	None stated	Crushed stone	Same citations as for fire clay
			Crushing, washing, sizing (screening), grading, recombining	Quartzite as a raw material used in manufacturing refractory products	House Hearings, 1950, p. 310 (App. B, pp. 413-414); pp. 793-794 (App. B, pp. 414-415); Senate Hearings pp. 415-416); House Hearings, 1953, p. 2089 (App
	Sand and gravel		—	Sand and gravel	House Hearings, 1953, p. 2069 (App. B, pp. 416-417)
	Shale		None stated	Shale	House Hearings, 1950, pp. 471-473 (App. B, pp. 418-1950, p. 704 (App. B, pp. 420-421); Senate Hearing pp. 422-423)
	Shells (oyster and clam)		Washing and screening	Shells	House Hearings, 1951, p. 1646 (App. B, p. 423); Sen 834-839 (App. B, pp. 424-427); House Hearings (App. B, pp. 431-432)
	Slate		Hand slicing	Slate (principally for roofing)	Senate Hearings, 1951, pp. 908-912, 1044, 2391 (App. H
	Sodium chloride (salt)	(1) Solid	Evaporation	Crude or "naked" salt	House Hearings, 1953, pp. 2044, 2046 (App. B, pp. 436
	Stone	(2) In brine	—	Salt	Same citations as for "limestone, ordinary"
	Wollastonite		Crushing and separation from other minerals	Crushed stone	Senate Hearings, 1951, pp. 896-897, 901 (App. B, pp. 4
				Wollastonite	

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BRIEF  
FOR THE  
RESPONDENT



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Office Supreme Court, U.S.

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JAMES R. DOWLING, Clerk

IN THE  
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1959

No. 513

UNITED STATES OF AMERICA,

*Petitioner,*

v.

CANNELTON SEWER PIPE COMPANY,

*Respondent.*

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF  
APPEALS FOR THE SEVENTH CIRCUIT

**BRIEF FOR THE RESPONDENT**

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IN THE  
SUPREME COURT OF THE UNITED STATES  
OCTOBER TERM, 1959

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No. 513

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UNITED STATES OF AMERICA,  
*Petitioner,*  
*v.*  
CANNELTON SEWER PIPE COMPANY,  
*Respondent.*

---

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF  
APPEALS FOR THE SEVENTH CIRCUIT

---

**BRIEF FOR THE RESPONDENT**

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**OPINIONS BELOW**

The District Court wrote no opinion. Its findings of fact and conclusions of law (R. 3-7) are not officially reported. The opinion of the Court of Appeals (R. 266-74) is reported at 268 F.2d 334.

**JURISDICTION**

The judgment of the Court of Appeals was entered on June 15, 1959. (R. 273) By order of Mr. Justice Clark, dated September 10, 1959, the time for petition-

ing for a writ of certiorari was extended to November 12, 1959. (R. 276) The petition for a writ of certiorari was filed on November 4, 1959, and was granted on December 14, 1959. (R. 276). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

### QUESTIONS PRESENTED

1. Whether the substantive questions raised by the Government are available for decision on this Record.

2. On the merits: The taxpayer produced burnt clay products (principally sewer pipe) from fire clay and shale which it mined from its underground mine. Except for a negligible amount of ground fire clay and shale, it sold no fire clay or shale, and there was no market which was economically available to it. Although fire clay and shale are sold in some locations, principally when produced as a by-product of strip-mining for coal, the great majority of fire clay and shale miners process their material into burnt clay products.

Under the statute, percentage depletion is computed as a percentage of the "gross income from mining." This term is defined as follows:

"The term 'mining' as used herein shall be considered to include ~~not merely~~ the extraction of the ores or minerals from the ground ~~but also~~ the ordinary treatment processes normally applied by mine owners or operators in order to obtain the *commercially marketable mineral product or products . . . .*" (Italics ours.)

The question is whether the "commercially marketable mineral product or products" of the taxpayer are the burnt clay products which the taxpayer could and



did sell, or whether they are the raw fire clay and shale which the taxpayer did not sell and could not commercially market.

### STATUTES AND REGULATIONS INVOLVED

The statutory provisions involved are Sections 23 (m), 23(n), and 114(b)(4) of the Internal Revenue Code of 1939. The regulation involved is Section 29.23(m)-1(f) of Treasury Regulations 111, as amended by T.D. 6031, 1953-2 CUM. BULL. 120. These provisions are set forth in Respondent's Appendix I, pages 121-28 *infra*.

### STATEMENT

Because the Government's statement of the case (Br. 3-5) is incomplete, we shall set forth the facts in the record of this case relevant to the issue presented here. The Government does not contend that any of the findings of fact of the District Court are erroneous or not sustained by the evidence. All of the facts stated herein are uncontroverted.

During its taxable year ended November 30, 1951, taxpayer was engaged in the business of mining fire clay and shale (in the proportions of 60% fire clay and 40% shale) from an underground mine which it owned and operated; transporting the minerals in trucks a distance of 1.5 miles to its plant in Cannelton, Indiana; and producing from such fire clay and shale vitrified sewer pipe, flue lining, and related vitrified products. (Fdgs. 7, 8; R. 4)

The processes applied by taxpayer to its fire clay and shale to obtain such products were grinding the clay; mixing it with water in a pugmill to form a

plastic mass; forming this mass in the shapes desired; drying these shapes to remove the added water; firing them in kilns to harden and vitrify them; and cooling the burnt clay products and removing them from the kilns. (R. 21-23, 95) All of the processes used and applied by taxpayer to the fire clay and shale which it mined and used were processes normally applied by mine owners or operators in producing such burnt clay products. (Fdg. 10; R. 5)

All clays and shales are not suitable for making sewer pipe. (R. 120) The clay used must have plasticity, particular drying qualities, and ability to withstand the high temperatures required for vitrification (i.e., firing to a very hard, glazy state). (R. 25-26, 121) Finding suitable clays requires considerable prospecting, and laboratory and production testing. (R. 26-27, 120-21)

The taxpayer mined fire clay and shale from beneath a vein of coal known as "Cannelton Coal" which is the lowest coal formation in Indiana (R. 115); the fire clay mined by taxpayer, known as the Cannelton clay, is the oldest (and deepest occurring) clay mined in Indiana (R. 33, 115-16) and yields the best sewer pipe which is made in Indiana. (R. 127) In 1951, no one else used the Cannelton formation of clay. (R. 33-34) The taxpayer's cost, without the allocation of any overhead, of extracting the fire clay and shale from its underground mine and transporting it to its plant, was \$2.418 per ton in 1951. (R. 39, 54; Gov't Ex. C, R. 56, 244)

Taxpayer has never sold any of its raw fire clay or

shale and has never purchased any fire clay or shale for use in its production. (Fdg. 11; R. 5) All of the fire clay and shale mined by taxpayer during its fiscal year 1951 (38,473 tons) was used by it in producing its burnt clay products, except for the sale of approximately 80 tons of ground fire clay and shale in bags at an average price of \$22.88 per ton. (Fdg. 9; R. 4-5)

During 1951, the other producers of clay products in the immediate Cannelton area did not sell or buy any raw clay and there were no mine owners or operators in such area who mined and sold clay to others. (R. 33) There were substantial sales of fire clay in Indiana in 1951, but 99% of these were in the area of Brazil, Indiana (R. 137), about 140 miles from Cannelton. (R. 44) The Court of Appeals correctly stated (R. 271) that these sales were made by companies falling into two categories: (1) "operators who engage primarily in strip mining of coal and, who, during their operations, strip bare so-called underclay which they sell as a by-product"; and (2) "those which mine underclay which has already been laid bare by previous strip mining operations." (R. 73, 82-83, 84, 88-89, 135-36, 148, 151, 152, 157, 159, 160) Several of these operators could not find a market for all the clay they had available for sale. (R. 136, 152, 160) As the Court of Appeals stated (R. 270, 272) out of the many companies mining fire clay and shale in Indiana in 1951, only seven producers of fire clay, two of whom also produced shale, sold their raw clay and shale without further processing (R. 72-73, 82-83, 136, 148, 151, 152, 157), and "the integrated miner-manufac-

turer was the rule rather than the exception in Indiana, in 1951." (R. 135)<sup>1</sup>

The mining costs of the strip miners in the Brazil area were low and, as the Court of Appeals stated (R. 271), "would be considerably below those of taxpayer which operated an underground mine." (R. 68, 89, 136, 159) The strip miners sold their fire clay at prices varying from approximately \$1.60 per ton to \$1.90 per ton delivered in the Brazil area (R. 80, 90, 149-50, 158) and shale was sold for \$1.00 per ton (R. 154), as compared with taxpayer's cost (without the allocation of any overhead) of \$2.418 per ton to mine the fire clay and shale and deliver it 1.5 miles to its plant. (R. 39, 54; Gov't Ex. C, R. 56, 244) The testimony showed that the cost of transporting clay from Cannelton to Brazil, a distance of 140 miles, varied from a low of \$4.58 per ton by rail (R. 37), to ~~\$5.50~~ per ton or more by truck. (R. 97; see R. 161)

On its original return for its fiscal year 1951, filed on February 11, 1952, taxpayer claimed no deduction for depletion. (R. 103)<sup>2</sup> Taxpayer filed an amended

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<sup>1</sup> The Government's Statement (Br. 4) says that "Substantial amounts of shale were also produced and sold in Indiana (R. 209), as well as in the United States generally." The Record citation contains no reference at all to sales of shale. The Record shows only two sellers of shale at Brazil, Indiana, both of whom were coal strip miners. (R. 82-83, 152)

We might also point out that the Bureau of Mines statistics as to sales of fire clay and shale, on which the Government relies in its Statement (Br. 4), are not in the Record.

<sup>2</sup> At that time, percentage depletion for fire clay and shale was not allowed, under the Internal Revenue Code, as to fiscal years ending in 1951. Revenue Act of 1951, § 319(c), 65 STAT. 497. By

return on August 15, 1952. (R. 249, 259) Before doing so, taxpayer was advised informally by the Chief of the Natural Resources Section of the Internal Revenue Service to compute its depletion deduction by using the selling price of its 80 tons of ground fire clay and shale and applying that price to its entire production. (R. 109-10) Upon audit of the taxpayer's return, it was allowed a deduction computed on the basis of including the costs and proportionate profits allocated to the processes applied through grinding and up to the pugmill and of excluding the costs and proportionate profits allocated to subsequent processes. (R. 95, 110-11)

Taxpayer in this suit claimed that its depletion deduction should be computed on the basis of the net sales of its burnt clay products, since they are its first commercially marketable mineral products. It also contended, in the alternative, that, if it was not entitled to compute its depletion deduction on such basis, it was entitled to compute its deduction on the basis of the actual selling price of the 80 tons of the ground fire clay and shale it actually sold. (R. 257)

The District Court found that there was no market for the fire clay and shale mined by taxpayer before it was processed into burnt clay products, except for negligible amounts of ground fire clay and shale sold in bags (Fdg. 12; R. 5), and held that taxpayer is entitled to compute its depletion deduction on the basis of the net sales of its burnt clay products. (Cone. 4; R. 6) The Court of Appeals affirmed. (R. 275)

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an amendment passed on July 21, 1952 (Pub. L. 594, 82d Cong., 2d Sess., § 5, 66 STAT. 820), it was allowed as of January 1, 1951, for such fiscal years.



## SUMMARY OF ARGUMENT

### Introduction

Section 114(b)(4)(A) of the Internal Revenue Code of 1939 provides that the depletion allowance, in the case of designated mines and other natural deposits, shall be a specified percentage of "the gross income from the property." Prior to 1943 the statute did not define "gross income from the property," and in administering the statute the Treasury began to try to restrict the depletion base in the same manner and for the same reasons as the Government now urges in this case. In order to prevent this, and over the Treasury's opposition, Congress in 1943 added to the Code, as Section 114(b)(4)(B), a definition of "gross income from the property." This definition provides that the term "gross income from the property" means the "gross income from mining" and that "mining" shall be considered to include "not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products." It is the meaning of this definition which is at issue in this case.

The Government does not challenge the determination of the courts below that there was no market economically available for the taxpayer's fire clay and shale before it was processed into sewer pipe and other burnt clay products. Nevertheless, presenting an issue not raised at the trial, the Government contends that the taxpayer's raw fire clay and shale were the

"commercially marketable" products because they were "fit for commercial or industrial use." It argues that the taxpayer's depletion allowance for its fire clay and shale (which it obtained by costly underground mining and which yielded the best sewer pipe made in Indiana) should in some way be determined with reference to raw fire clay and shale, which were sold as by-products by coal strip miners 140 miles away.

In urging this result, the Government asks this Court to overturn decisions in 54 cases by the lower Federal courts, including several Courts of Appeals, the Tax Court, and numerous District Courts. A chart summarizing the cases is included as Part E of Respondent's Appendix II, pp. 173-81.

# I

The case raised by the Government in this Court is not available to it on this Record. This case started out in the District Court as a very simple case. One of the issues raised by the pleadings, the pre-trial order, the opening statement of Government counsel at the trial, and the Government's brief—the only question relevant to the case at this stage—was whether there was a market economically available to the taxpayer for its fire clay and shale.

The taxpayer proved overwhelmingly that, whether there is a market for fire clay and shale elsewhere or not, the taxpayer's fire clay and shale were not "commercially marketable" because they could not economically be brought to any such market for sale. Indeed, it developed at the trial that the Government's case was apparently largely based on an error, a misplaced decimal point.

The Government now concedes "that taxpayer's mining and transportation costs were so high that it could not profitably market the minerals in crude form." (Gov't Br. 6; see also Gov't Br. 21, middle of the page.) The Government now raises a wholly different issue, never raised at the trial. It takes what may be called a "national market" approach, and uses such phrases as "basic product sold by the particular mining industry" (Pet. for Cert. 15) and "fit for commercial or industrial use." (Br. 21, 85, and elsewhere.) The Record contains no evidence about these things. No such issues were raised in the District Court. If such issues had been raised they would have involved the production of voluminous evidence, and the factual material now available to the Court would be entirely different. The question which the Government now raises cannot fairly be decided, and should not be decided, on this Record, made on another issue.

What the Government is, in effect, asking here is for a new trial. But it is not entitled to a new trial unless the District Judge erred in deciding the issues which the Government presented to him at the trial which has been held. The Government has had its day in court.

In default of a Record supporting the issues it now raises, the Government here relies almost entirely on "Official Statistics" which were never presented to the District Court, were not offered in evidence in the District Court, and are not included in the Record in this case. If the Court can take judicial notice of these reports, it can also take judicial notice of the way in which they are prepared, and of the inadequa-

cies and inaccuracies which are inherent in such material. They are surely a shaky foundation on which to rest the decision of a case involving "close to a billion dollars," which the Government now says this case is.

The findings made by the District Court on the evidence and issues presented to it are not now contested by the Government. That should be an end of this case. On this Record, as made on the issue presented by Government counsel, the judgment below should be affirmed without consideration by the Court of the new arguments now presented by the Government, which were never presented to the District Court. In the alternative, the writ of certiorari should be dismissed. *Rice v. Sioux City Memorial Park Cemetery, Inc.*, 349 U.S. 70, 77-79 (1955); *Tyrrell v. District of Columbia*, 243 U.S. 1 (1917).

## II

The meaning of the statute necessarily turns upon the meaning of "the commercially marketable mineral product or products," since the "ordinary treatment processes" included in the statutory definition of mining are those "normally applied" by mine operators *in order to obtain* "the commercially marketable mineral product or products."

A. In order for a product to be "commercially marketable" within the ordinary meaning of that term, there must be an actual, continuing, regular opportunity to sell it on a practical business basis. In all the cases the courts have held that Congress intended the term to have its ordinary meaning.

The Government tries to write "commercially marketable" out of the statute by substituting for it, "fit for commercial or industrial use," a phrase that has a quite different meaning. Its position is that the other language of the statute shows a Congressional intent to exclude from "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products" any process which is "manufacturing" as the Government defines that term. The statute provides no basis for such an interpretation. If Congress had intended to exclude processes which might be called "manufacturing," it could have said so; as a matter of fact, however, nowhere in the statute did it use the word "manufacturing." Furthermore, Congress specifically listed in the statute as "ordinary treatment processes" certain processes (*e.g.*, cyanidation, leaching) which are "manufacturing" within the Government's definition of that term. Congress obviously intended to adopt a practical rule for computing percentage depletion based on using the selling price of the "commercially marketable mineral product or products," whether or not such product or products might be termed "manufactured."

B. The wording and structure of the statute show that "the commercially marketable mineral product or products" refers to the first product or products actually obtained by the taxpayer in his processing of his mineral which he has an opportunity to sell on a commercial basis. Section 114(b)(4)(B) defines "gross income from the property," which obviously refers to the particular taxpayer's gross income



from his mining operations. These are defined specially to include not merely the extraction by the taxpayer of its fire clay and shale from the ground but also certain processes applied "in order to obtain the commercially marketable mineral product or products." The plural reference to "products" shows that Congress did *not* intend to establish arbitrarily a single "basic product" for each mineral, as the Government contends.

Congress' intention that "the commercially marketable mineral product or products" may be different for miners of the same mineral is also shown by the lists of ordinary treatment processes in the statute. In the case of certain minerals and ores, the statute lists processes which are not always applied to such minerals; when applied, they yield products different from those sold in substantial amounts by other miners of the same minerals who do not apply them.

Further evidence of Congress' intent is found in its choice of the words, "commercially marketable." The determination of commercial marketability required by the statute is not one which can be made satisfactorily on an industry-wide basis for each class of minerals. In applying the statute to varied factual situations in the complex field of mining, the courts have had to deal with the geologic fact that there are different grades of the same mineral with different utility and value and with the economic fact that the market situation for mineral products varies materially. They have recognized that the determination of the commercially marketable mineral product or products must be made on the basis of such facts in order to carry out the Congressional purpose and that therefore there is not nec-

essarily a single commercially marketable product for each class of mineral.

Under the interpretation of the statute adopted by the court below and by the courts in all the many cases involving the question, the identity of "the commercially marketable mineral product or products" is a question of fact to be resolved by determining the first such product or products actually obtained by the taxpayer. Once that determination is made, then the processes which the taxpayer actually applies and which are the "ordinary treatment processes normally applied by mine owners or operators" in order to obtain such product or products are to be considered a part of mining.

C. The Government does not challenge the District Court's finding, endorsed by the Court of Appeals, that there was no market in which the taxpayer could have sold its fire clay and shale on a profitable basis, before it was processed into sewer pipe and other burnt clay products. These, then, were the taxpayer's commercially marketable mineral products.

The District Court also found that all of the processes applied by the taxpayer were the processes normally applied by mine owners or operators to obtain such burnt clay products. This finding is not challenged by the Government.

Therefore, the taxpayer is entitled under the statute to compute its deduction for depletion of its deposits of fire clay and shale on the basis of the selling price of its burnt clay products.

D. Even if the commercially marketable mineral product or products are to be determined on an

industry-wide basis, as the Government contends, the judgment should be affirmed, since miners of fire clay and shale normally are required to process such minerals into burnt clay products to make them marketable.

If Congress has established an industry-wide test, then "mining" includes the processes "normally applied" by owners or operators of fire clay and shale mines in order to obtain commercially marketable products. What they "normally" do must be what they do usually and ordinarily. Because the Government agreed with the taxpayer at the trial that the issue was whether the *taxpayer's* clay was commercially marketable, there is no evidence in the record to show what processes producers of fire clay and shale in the country as a whole normally and ordinarily apply to obtain their commercially marketable products. However, as the Court of Appeals concluded, the record does show that in Indiana, where the taxpayer's mine is located, "the integrated miner-manufacturer was the rule rather than the exception" in 1951.

The statistics quoted in the Government's brief, as well as the findings in other cases where the Government did raise the issue, show that the same was true in the country as a whole.

### III

Although the Government devotes most of its brief (pp. 9-17, 35-80) to an attempt to show that the legislative history of percentage depletion requires its interpretation of the statute, the fact is that the legislative history shows that: (1) Congress intended to

adopt the commercially marketable products rule, although recognizing that various miners of the same ore or mineral might thereby have different bases for depletion; and (2) Congress, in enacting and adhering to that rule, has repeatedly rejected the Government's position here and its arguments in support thereof.

Ever since Congress first enacted discovery value depletion in the Revenue Act of 1918, it has allowed a depletion deduction greater than a taxpayer's actual investment or cost in his mineral deposit, in order to provide an incentive to discover, develop, and operate deposits of natural resources. Percentage depletion, which has replaced discovery value depletion, allows a deduction bearing little or no relation to investment. Although the Treasury has long fought percentage depletion as over-generous and has repeatedly attacked the commercially marketable products rule, Congress favors percentage depletion and has repeatedly refused to accede to the Treasury's wishes.

A. Percentage depletion provides an easily computed deduction, once the dollar base (to which the applicable percentage is applied) has been determined. Congress has elected to use the commercially marketable products rule as a simple method to determine that base: the taxpayer can readily determine the selling price of such products (if he sells them) or their established market value (if he processes them further). In looking for a way to avoid the difficulties of valuation inherent in discovery value depletion, Congress chose this simple rule in preference to others which would have given a greater equality of treatment to miners of the same mineral.

B. Section 114(b)(4)(B), which specifically enacts the commercially marketable products rule and which is the provision to be interpreted in this case, was added to the Code by the Revenue Act of 1943. The Report of the Finance Committee, which added this provision to the Bill, makes its meaning clear, stating that it is intended "to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation." This Report also states that it "expresses the congressional intent of these provisions as first included in the law, and is "in accord with the original regulations and the Bureau practices and procedures thereunder." Consequently, to understand fully this legislative history, it is necessary to review the history of the Revenue Act of 1932 and the original interpretation of the depletion provisions of that Act.

In 1932, Congress granted percentage depletion to coal, sulfur, and metal mines. Guidance as to Congress' intent is supplied by the so-called "Shepherd Report" which, in 1929, proposed percentage depletion for metal mines on the basis that Congress adopted in 1932; this Report reviewed the market situation as to the various ores and recommended defining "gross income from the property" with reference to marketability. Before the Treasury released its regulations under the 1932 Act, the mining industry pointed out that they did not express the Congressional intent. The Treasury admitted that they did not, but, since the regulations were printed, they were released with the understanding that they would *not* be applied as writ-



ten, but would instead be applied to give effect to the commercially marketable products rule. In so applying them, however, the Treasury did not treat all producers of an ore in the same way; for example, a miner of gold ore who used cyanidation (an allowed process) or a miner of copper ore who used leaching (also allowed) was permitted to compute his allowance on a more refined product than miners who used smelting (a disallowed process; ores to be smelted are commercially marketable in the concentrate form before smelting).

About 1940, the Treasury changed its position and disallowed certain processes, apparently making the same theoretical distinction between "mining" and "manufacturing" as it urges here. Thus, it wanted to exclude metallurgical processes effecting a chemical change which altered the character of the mineral and feared that allowing some such processes (as it had been doing) would permit all "finished" products, such as steel, to be used to determine the depletion base; it justified its position on the ground of achieving equality and theorized that a mine owner who used these metallurgical processes supplied his own market for the ore.

When the Treasury's change in policy was called to Congress' attention in 1942, it did not act because the Treasury stated that it would correct the situation administratively. However, it did not do so, and Congress, in the Revenue Act of 1943, added Section 114 (b)(4)(B) to the Code, using the language to be interpreted here, which has no counterpart in any prior statute, regulation, or ruling. It also specifically listed

in the statute the metallurgical processes (including cyanidation and leaching) which the Treasury began to disallow in 1940. Thus, Congress clearly adopted the commercially marketable products rule which it had originally intended and which the Treasury had originally applied under its regulations.

C. Beginning in 1942, Congress granted percentage depletion to additional minerals and, finally, in 1954, granted it to all minerals. The legislative history shows that Congress, in so doing, has intended to provide an incentive to discover and develop deposits of these various minerals and has recognized that it is not just providing a return of the mine owner's capital. It is also obvious that Congress has adhered to the commercially marketable products rule, in the face of the Treasury's repeated attacks on it.

1. In 1950, Congress added to "mining" transportation from the point of extraction to the mill or plant where the ordinary treatment processes are applied, in order to insure the statutory scheme of using the selling price of the commercially marketable products as the depletion base. The Treasury at the time was trying to whittle away at that base by disallowing transportation after having previously allowed it.

2. Fire clay and shale were granted percentage depletion by the Revenue Act of 1951. The Government cannot point to any statement in the legislative history showing that Congress did not intend the depletion deduction for these minerals to be computed under the commercially marketable products rule, just as it is computed for all other minerals. A subsequent letter by Senator George, Chairman of the Finance Commit-

tee in 1951, written with reference to "brick and tile clay" (which was also granted percentage depletion in 1951) states that "... [T]he statute defining mining for purposes of computing depletion allowance for federal income and excess profits tax purposes does not exclude manufacturing processes so long as they are ordinary processes normally and necessarily used in obtaining commercially marketable mineral products," and that the Finance Committee was told that "manufacturing" processes would be included in "mining" as to that mineral.

3. In 1954, Congress at the request of industry representatives amplified the ordinary treatment processes specifically listed in the statute by adding certain processes for talc, magnesite, phosphate rock, and coal. On the other hand, when the Treasury sought legislation, in 1954, to exclude specifically the "manufacturing" processes applied to brick and tile clay, Congress refused to enact such legislation.

4. In 1958, the Treasury asked Congress to change the commercially marketable products rule by specifically excluding the "manufacturing" processes applied to clay and to the minerals used for cement. Congress took no action on this proposal.

5. In 1959, the Treasury asked Congress to abolish the commercially marketable products rule completely and to substitute a rule based on its distinction between "mining" and "manufacturing." The Ways and Means Committee held five days of hearings on this proposal. At these hearings, the Treasury made the same arguments as it makes here: it urged that only "mining" processes as opposed to "manufacturing"

processes should be allowed in determining the depletion base; it argued that the statute creates discrimination among taxpayers (accepting the interpretation that different taxpayers have different commercially marketable products) and encourages integration; and it stated that the present statute gives "excessive" allowances, presenting the same charts purporting to show the amounts of revenue involved as it attached to its Petition for Certiorari here.

The Treasury's proposal was received with a general lack of enthusiasm. One member of the committee feared that departure from the established commercially marketable products rule might develop "more confusion" and cause "a great deal of litigation over this cut-off point," instead of "bringing about uniformity of treatment." Another expressed the thought that "we might advisedly retain something that gives us an element of certainty rather than adopt the terrific uncertainty that we would find from the approval of a new approach to this question." It was also feared that, because of its uncertainties, the proposal would put too much power in the hands of the Treasury.

No further action was taken on the Treasury's proposal.

D. In summary, Congress has consistently used the commercially marketable products rule to supply the base for computing percentage depletion and has, in fact, always regarded it as central to its concept of percentage depletion. Congress enacted Section 114 (b)(4)(B), because the Treasury was departing from this rule. Ever since enacting that section, Congress has steadfastly adhered to the commercially market-

able products rule in spite of the Treasury's attacks on it, specifically including "transportation" in "mining" in 1950 to preserve that rule, and refusing to change the rule when the Treasury asked it to do so in 1954, 1958, and 1959

#### IV

A. The Government's position here that income from "manufacturing" processes cannot be included in computing the depletion base is not new. When the Treasury first adopted such position, Congress negated it by enacting Section 114(b)(4)(B). The Treasury revived it in 1953, by an amendment to its regulations. This amendment was promptly challenged in court and the Government tried to square its position with the statutory language by arguing that "commercially marketable" means "ready for manufacture." As it lost case after case, it turned to other words in the statute to justify its interpretation, emphasizing at various times the word "mineral" which appears before "product or products" and "normally applied by mine owners or operators." Now, after having been unsuccessful with all these arguments in the lower courts, it returns to the position that "commercially marketable" means "fit for commercial or industrial use," although it did not so argue in the courts below or in its Petition for Certiorari.

The Government's difficulty and vacillation in attempting to square its basic position (distinguishing "mining" from "manufacturing") with the statute shows it is trying to read into the statute something which is not there.



B. The weakness of the Government's case is shown by its failure to take a position in its brief as to how the statute should be applied to this taxpayer; it merely says (Br. 80, Heading III) that taxpayer's deduction must be computed "with reference to" raw fire clay and shale, and asks (Br. 91) ~~that~~ this Court reverse and remand so that the taxpayer's "'gross income from mining' may be determined in the light of the correct legal criteria."

Under the Treasury regulation, either a "market or field price" or "proportionate profits" method would be used.

Any use of a "market or field price" presents many unanswered questions. Is the price determined for a "local" area (even though there is no area in which taxpayer could sell its fire clay and shale on any practical, business basis) or for the country as a whole? As of what date is the price computed? For fire clay, is it an average price for all kinds of fire clay, which vary widely in utility and value? Are the prices of fire clay and shale sold as by-products by coal strip miners relevant in determining the depletion deduction of producers of fire clay and shale from underground mines?

In the District Court, the Government discarded the "proportionate profits" method, describing it as "abrogated" and "abandoned," and its brief does not assert that it should be used in this case.

C. Application of the Government's theories to other factual situations would cause confusion and illogical results.

For example, there are situations (involved in decided cases) where two commercially marketable products are obtained by entirely different processing from the same deposit of the same mineral, not marketable in crude form, and where one of those products is more valuable because of the greater value of the raw mineral used to produce it. How would "gross income from mining" be computed in the case of the mineral used for that more expensive product? Under the Government's approach, it would seem that the taxpayer's deduction might well be smaller in the case of the mineral used for the more valuable product, because only the processes applied to obtain the cheaper product (the "basic" product) would be included in "mining" and thus none of the processes applied to obtain the more expensive one would be so included. If, as it has in some cases, the Government should say that the depletion base for the more valuable product is the market price of the cheaper product, there would be problems of applying the statutory limitation of the deduction to 50% of the "net income of the taxpayer . . . from the property." If a miner of such a mineral produced only the more valuable product, how would he compute the "net income" that he *would* have realized if he had applied the entirely different processes that others use to obtain the "basic" product and thus had incurred entirely different costs?

Furthermore, how would the basic mineral product be determined for minerals such as brick and tile clay for which there is no market anywhere before "manufacturing" processes are applied? When are such minerals "fit for commercial or industrial use"? The

Government says here (Br. 18) that a market somewhere in the country provides "conclusive proof" that a mineral has reached this stage, but recognizes that other tests will be needed when there is no such market. If the first process after extraction is not allowed, there are no "ordinary treatment processes"; if it is included, there is no logical or reasonable basis for saying industrial use begins with any succeeding process.

Any explanation of how to compute the deduction in these situations will of necessity involve arbitrary distinctions and theoretical computations which will produce results inconsistent with the legislative intent.

D. The Government urges this Court to consider what it calls the "extreme results" of the commercially marketable products rule.

The Government claims the rule results in "sharp disparities and widespread discrimination" between the "integrated miner" and others, but the illustrations which it gives do not show results inconsistent with the intention of Congress. For example, it points to a contractor (described by the Government as a "non-integrated miner in the same area") who extracted and hauled clay and shale for the mine owner at a rate per ton for his services. The Government says this contractor was entitled to a depletion allowance of only 15 cents per ton. Actually he was not entitled to any depletion allowance, since he had no economic interest in the clay and shale deposits.

The Government's assertion that the holding below encourages "vertical integration" on an "inefficient basis" assumes without justification that the taxpayer's mine was inefficient. The statute as written may well encourage the development of mines which otherwise

would not be developed—just as Congress intended. Whether it will lead to the merger of existing business entities is a complicated economic question as to which assumptions are unreliable. Any such possibility has not alarmed Congress, which has rejected the Treasury's pleas to eliminate the commercially marketable products rule.

The Government's claims as to "virtually limitless" possibilities for depletion allowances and "enormous" potential impact upon the revenue under the commercially marketable products rule are unsupported. The applicability of the rule depends entirely on the factual question of commercial marketability. In its predictions, the Government assumes that various minerals cannot be sold commercially until they are processed into "manufactured products," without analyzing the facts so that this Court may consider whether such assumptions have any foundation under the statute as construed by the courts.

The Government's complaint about the administrative problems under the commercially marketable products rule exaggerates the difficulties, ignores the administrative problems which would result from the Government's theory, and simply reflects the Treasury's desire for restoration of the broad administrative discretion in determining "gross income from the property" which Congress took away in enacting the statutory definition of that term.

In sum and substance, the Government now asks this Court to do what Congress has steadfastly refused to do, and this is an area which is peculiarly one for legislative judgment.

## ARGUMENT

### Introduction

The Government argues that the decision of the Court of Appeals should be reversed because "two fundamental and closely related propositions" which it adopted are erroneous.<sup>1</sup> By so arguing, the Government asks this Court to overrule decisions in 54 cases, decided by a total of 52 Federal judges (25 Court of Appeals judges,<sup>2</sup> 26 District Court judges, and 4 Tax Court judges), over a period of 16 years.<sup>2</sup> In this lengthy and extensive litigation, the Government has obtained only one decision supporting its position here; and that was by a District Judge, who was reversed by the Court of Appeals, and who based his decision on grounds which the Government does not even present in its brief. *The Government does not, and cannot, cite one decision to support its position here.*

Furthermore, the Government asks this Court to overrule these cases after repeated, unsuccessful attempts to have Congress change the statutory provisions so as to adopt the Government's position here. In 1954, it tried unsuccessfully to obtain an amend-

<sup>1</sup> These propositions are stated as follows (Gov't Br. 21-22):

"(1) that the product with reference to which the gross income from mining is computed varies according to the particular product which the taxpayer, on the basis of his particular operation, finds it profitable to sell; (2) that the phrase 'ordinary treatment processes normally applied by mine owners or operators' may be extended to take in processes which could never be employed by one who is strictly a mine operator and can only be utilized by one who is also a manufacturer."

<sup>2</sup> A complete list of these cases, together with the names of the judges who decided them, is set forth in Part E of our Appendix II, pp. 173-81.



ment enacting its position as to brick and tile clay; in 1958, it tried unsuccessfully to obtain an amendment enacting its position as to clay and as to minerals used for cement. In 1959, it submitted a broader legislative proposal covering all minerals and completely eliminating the "commercially marketable mineral product or products" test of the present statute. The Ways and Means Committee held five days of hearings, but has not reported a bill.

Thus, the Government is now urging this Court to upset an unusually long and unanimous line of authority, after three unsuccessful attempts to obtain legislation. In so doing, it presents to this Court a synthesis of most of its arguments which the lower courts have unanimously rejected, relying on (1) the statutory language and (2) the legislative history, but without ever explaining how it believes the depletion deduction should be computed in this or other cases. As we shall show below, the statutory language and legislative history have been correctly interpreted by the many lower courts which have carefully and repeatedly considered them.

# I

THE CASE RAISED BY THE GOVERNMENT IN THIS COURT IS  
NOT AVAILABLE TO IT ON THIS RECORD

This case started out in the District Court as a very simple case, involving two factual issues. These were:

1. Whether the taxpayer's clay was fire clay; and
2. Whether there was a market which was economically available to the taxpayer.

Both the taxpayer and the Government tried the case on this basis. The taxpayer presented only three witnesses, two officers of the company in person, and one expert by deposition. Through this evidence, it proved overwhelmingly that its clay is fire clay. The District Court so found, and the Government did not appeal from that decision. That question, to which much of the Record is devoted, is no longer in the case.

In addition, the taxpayer proved overwhelmingly that, whether there is a market for shale or fire clay in Brazil, Indiana, or not, the taxpayer's shale and fire clay were not "commercially marketable" in Brazil, because they could not economically be brought there for sale. The prices shown by the Government's evidence for sales in Brazil range from \$1.00 per ton for shale (R. 154) to approximately \$1.60 to \$1.90 per ton for some types of clay. (R. 80, 90, 149-50, 158) The evidence clearly showed that the taxpayer's cost of extracting its shale and clay from the ground in 1951 was \$2.418 a ton (R. 39), and that the cost of transportation to Brazil varied from a low of \$4.58 per ton by rail (R. 37) to \$5.50 or more per ton by truck. (R. 97; see R. 161) On this basis, the District Court rejected the Government's contention that the taxpayer's shale and clay were commercially marketable in Brazil, or anywhere.

Indeed, at the trial it developed that the Government's whole case was apparently based on a misplaced decimal point. In his opening statement, counsel for the Government stated (R. 17) that:

"The economics of the situation will also be a matter of proof and the Government will offer evidence to show the average cost, including a profit, of transporting clay is 1.8 cents per ton mile. The Government will further demonstrate at that price, comparing with the price that was paid by the taxpayer to haul clay, they could haul clay considerable distances."

When the Government's witness, Charles N. Smith, appeared, he gave such testimony. He testified explicitly that the cost "would be about 1.8 cents." (R. 84) He held to this figure on cross examination (R. 85), but weakened towards the end. (R. 87) Then, on the following day, counsel for the Government stood up in court and said (R. 161):

"Mr. Smith, who testified yesterday, has examined the computations which he made, and states to me that he made a misplacement of the decimal point, and it should be 18 cents per ton mile, rather than 1.8 on the short-haul distances."

The Record then continues (R. 161):

"Mr. Travis: (For Pltf.) We will stipulate the 18 cents is correct, the correct figure.

"Mr. Friesen: (For Deft.) Mr. Smith came back to make the record clear."

It was also testified that this hauling cost did not include a profit, but was "strictly the cost." (R. 85)

On the case which the Government now raises, the cost of transportation between Cannelton and Brazil, or any place else, is utterly irrelevant. The Govern-

ment now concedes the only issue remaining which was in the case at the trial, for it expressly states "that taxpayer's mining and transportation costs were so high that it could not profitably market the minerals in crude form." (Govt. Br. 6; see also Gov't Br. 21, middle of the page.) The Government now raises a wholly different issue, never raised at the trial, namely, that there is a "basic product sold by the particular mining industry" (Pet. for Cert. 15), or that the depletion allowance is to be determined by "sales of fire clay on a national scale" (Gov't Br. 82), or by "national sales of shale." (Gov't Br. 83) Thus, the Government now takes what may be called a "national market" approach, and here contends that the taxpayer's depletion allowance should, in some way, be determined by this national market to which it concededly could get no access. This may not be exactly the Government's position now; but whatever it is, it is different from anything which was raised in or presented to the District Court.

The Record contains no evidence about "basic product sold by the particular mining industry," or about other aspects of the fire clay and shale industries on a national basis. It contains no evidence about the application of "fit for commercial or industrial use" (Gov't Br. 21, 85), or any other of the several phrases on which the Government now relies in its interpretation of the statute. No such issues were raised in the District Court. Neither of these terms was even mentioned by Government counsel in the District Court, either in pleadings, pre-trial conference, opening statement, at

the trial, or in argument or brief.<sup>1</sup> Yet, it is obvious that they are the keys to the contentions which the Government is now making.

If such issues had been raised, they would have involved the production of voluminous evidence. Evidence would have to be introduced to show not only the circumstances and conditions, and facts about sales, in Brazil, Indiana, but also at many other places in the United States, and perhaps elsewhere in the world. In addition, evidence would be introduced to show that types of clay and shale are not fungible, that there are many variations and differences in quality, consistency, chemical content, color, durability, heat resistance, and so on, in various clays, so that the mere fact that some fire clay or shale of some quality and character was sold some place would not mean that there was a "market" which was relevant to this particular taxpayer, whose special quality of clay and shale resulted in "the best sewer pipe that is made in Indiana." (R. 127)

If these issues of a "national market" or of "fit for commercial or industrial use" had been raised at the trial, the Record in this case and the factual material available to the Court would thus be entirely different. The question which the Government now

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<sup>1</sup> In its Reply Brief in the Court of Appeals below in this case, the Government expressly recognized this as to "national market." It said (p. 15): "But we had not heretofore thought it was necessary for the Court to decide the national versus area-wide marketability question in this case, and accordingly did not argue it either in the trial court or in our main brief in this Court." (Italics ours.) Clearly the present position of the Government is an afterthought.



raises cannot fairly be decided, and should not be decided, on this Record, made on another issue. This case, as the Record clearly shows, is a simple case, presented to the District Court on simple factual issues. These issues related at most to a local market in Brazil, Indiana, and they were settled when it was shown that there was no market there which was relevant to this taxpayer, since the taxpayer could not get to it. That market, if it is a market in any appropriate sense, is no more relevant to this taxpayer than if it had been in Maine or in Hawaii. The economics of the situation kept the taxpayer's clay and shale out of Brazil as effectively as it kept it out of New York or Seattle. The Government did argue "market or field price," but the evidence shows that there was no "market or field price" for any sort of clay and shale in an area which included Cannelton. The case which the Government raised on these points, through pleadings, pre-trial conference and order, opening statement, evidence and argument, was a fairly simple case, and was fully met by the taxpayer's evidence at the trial, and through cross-examination of the Government's witnesses.

The Government now raises a very complex case, involving complicated factual and economic issues on which the Government now says that "close to a billion dollars" turns. (Reply Brief on Pet. for Cert. 6) No such case was ever presented to the District Court. Would a billion dollar case be tried with three witnesses for the plaintiff, in two days?

Indeed, the Government concedes here, as it did in the court below (see note 1, p. 32 *supra*), that this Rec-

ord does not raise the questions it now wants decided. It does not ask for a reversal, with the taxpayer's complaint to be dismissed. On the contrary, its prayer (Gov't Br. 91) is that "the judgment of the Court of Appeals should be reversed and the cause remanded so the taxpayer's 'gross income from mining' may be determined in the light of the correct legal criteria." This, in effect, is a request for a new trial. But the Government is not entitled to a new trial unless the District Judge erred in deciding the issues which the Government presented to him at the trial which has been held. The District Judge made no such error on the issues and arguments which the Government tendered him. The Government has had its day in court. It is not entitled to another day in court in order that it may present a new and different case, based on issues which it never raised when this case was tried in the District Court.

The Government now, in default of a Record supporting the issues it now raises, relies almost entirely on "Official Statistics" which were not offered as evidence in the District Court, were never presented to the District Court, and are not included in the Record in this case. There are two such items, first, the "Minerals Yearbook" (1951), U. S. Bureau of Mines, Department of the Interior, and second, the "1954 Census of Mineral Industries," U. S. Bureau of the Census, Department of Commerce, both cited and relied on at pages 82 and 83 of the Government's brief.

This material, not in the Record, and never presented to the District Court, is surely a shaky foundation on which to rest the decision of a case involving "close

to a billion dollars." If the Court can take judicial notice of these reports, it can take judicial notice of the way in which they are prepared, which is by the distribution of questionnaires through the mail, often filled out by clerical or subordinate employees.<sup>2</sup> Many questions necessarily lurk in such a report. What, for example, is the definition of "fire clay"? The Record in this case shows that the meaning of that term is quite uncertain. Is it clear that all of those who responded to the questionnaires used the same meaning, or made the distinctions which are necessary if the data are to be useful in a case like this? What is the meaning of "sale" as used in these reports? Does it include sales between subsidiary and parent, or between divisions of the same company? How many of the sales were by strip miners or by miners who have underground mines? Is it clear that these two types of producers are in "the same industry"? Were the taxpayer's clay and shale usable for the same purposes for which the sales reported in these statistical reports were made? A market for materials with which the taxpayer's fire clay and shale are not reasonably interchangeable for the same purposes would not be relevant. Cf. *United States v. duPont & Co.*, 351 U. S. 377, at 394-5 (1956). The question of the extent to which materials and products are substantially fungible in this sense in the "national market" is clearly a question of fact, on which the factual presentation when the issue

<sup>2</sup> The Record does contain evidence that the reports obtained from the producers are compiled by a person who "is not geologically or ceramically trained." (R. 137). See also R. 83, showing the inadequate way the original reports are made.

is raised would clearly be extensive.<sup>3</sup> There is no evidence on this in this Record because no such issue was raised in the District Court.<sup>4</sup>

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The issue in this case was originally raised by the following allegation in the complaint (R. 252) which was denied by the answer:

“Except for negligible amounts, there is no market for the fire clay and shale mined by plaintiff before it is put in the form of vitrified sewer pipe.”

No motion to dismiss was made for failure to state a cause of action on which relief could be granted.

A pre-trial conference was held on January 7, 1958, and, thereafter, a pre-trial order was entered which was approved by both counsel. This pre-trial order was never modified, and no request was made by the Government to modify it.

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<sup>3</sup> “No two clays are exactly alike; and it is seldom possible to substitute one clay for another in industry without considerable experimentation, even though extensive research data have been established.” U. S. BUREAU OF MINES, DEPT OF INTERIOR, BULL. NO. 556, MINERAL FACTS AND PROBLEMS 187 (1956).

<sup>4</sup> The barrenness of the Record on these issues now essential to the Government's case is shown by reference to the one paragraph in its Statement (Br. 4) which is devoted to the factual basis of its present contentions. There is there a reference to a Government Report which is not in the Record. Most of the other references are indirect references to this Report. One Record reference is contained in the following statement: “Substantial amounts of shale were also produced and sold in Indiana (R. 209) . . .” Reference to R. 209 shows that it contains nothing whatever about sales of shale.

Paragraphs II and IV of this pre-trial order are relevant, and appear at R. 264 and 265. They read as follows:

“II

“Counsel for the defendant represented to the court that the defendant, through its Internal Revenue Service, had initiated as of this date a survey regarding the sales of shale and fire clay in a certain marketing area which would include the location of the plaintiff's mine and factory, to determine whether or not the defendant will claim in this cause of action *that plaintiff has a market for the clay which it mines prior to being put in the form of finished vitrified sewer pipe* and other related products which are made and sold by the plaintiff; and further, that if the defendant determined that *there was such a market, then an additional survey would be made to determine the market value of the clay mined by plaintiff at the point where the defendant determined that there was a market for the clay.*

“Counsel for the defendant further represented that if it were determined as a result of the survey that there was no market for clay and shale of the type mined or used by plaintiff prior to its being put in finished form ready for sale, then plaintiff's claims as alleged in plaintiff's complaint would be recommended for administrative refund by the Internal Revenue Service of defendant.



## "IV

"If this cause of action is to be tried by the court, it was agreed between the parties that the *only issues of fact* which would have to be presented to the court *would be first, whether the plaintiff has any 'commercially marketable product or products' from the shale and clay which it mines prior to the finished vitrified sewer pipe and other products* which plaintiff produces and sells; and, *second, what is the value of such 'commercially marketable product or products' if it is determined that plaintiff has such a product or products prior to the completed vitrified sewer pipe and other products which plaintiff makes and sells.*" (Italics ours.)

That the issue in the case was the narrow one relating to this particular taxpayer was again made clear in the opening statement by the Government's counsel, where he said that the issue was (R. 16):

"What is the first commercially marketable mineral product of this particular mine owner's mine or operator's mine?"

After the trial of the case the District Court made its Findings of Fact in accordance with the issues framed by the pre-trial order. Findings 12 and 13 are as follows (R. 5):

"12. There was no market for the fire clay and shale mined by plaintiff before it was processed into said products, except for negligible amounts of fire clay and shale sold in bags.

"13. The first 'commercially marketable' mineral product' of the fire clay and shale mined by plaintiff during the years in question was the said finished products."

These findings have never been attacked by the Government as not being sustained by the evidence.

The findings made by the District Court on the evidence and issues presented to it are not now contested by the Government. Thus, the Government now admits that the District Court correctly decided the issue as it was presented and tried by Government counsel.

That should be an end of this case. We submit that on this Record, as made on the issue presented by Government counsel, and since the Government has conceded that the only factual issues presented to the District Court were correctly decided, the judgment below should be affirmed, without consideration by this Court of the new arguments now presented by the Government which were never presented to the District Court.<sup>5</sup> In the alternative, the writ of certiorari should be dismissed as having been improvidently granted. See *Rice v. Sioux City Memorial Park Cemetery, Inc.*, 349 U.S. 70, 77-79 (1955); *Tyrrell v. District of Columbia*, 243 U.S. 1 (1917).

In the *Tyrrell* case, certiorari was granted on the basis

<sup>5</sup> This question was fully presented to the Court of Appeals by the taxpayer in its brief in that court (pp. 17-24). The taxpayer has never waived its contention that the broad issues now raised—clearly involving substantial bases of fact not developed in this Record—were never raised at the trial in this case. The taxpayer should not be prejudiced because the Court of Appeals chose to put its decision on broader grounds.

of a petition which stated that the Court of Appeals ignored, or was under misapprehension about, a line of cases holding that the District of Columbia was responsible for torts of its employees. On examining the record, after oral argument, this Court found (243 U.S. at 4) "that the question upon which the certiorari was prayed . . . does not arise on the record and is not open for consideration." The Record showed that the trial court had charged the jury that the District could not be responsible for an isolated act of negligence, but if responsible at all was liable only for the maintenance of a nuisance. No exception was taken on the issue of an "isolated act of negligence." This Court dismissed the writ of certiorari, "since that question, under the state of the record, was not before the lower court and would not be open for our consideration. . . ." 243 U.S. at 6. See also *Furness, Withy & Co. v. Yang-Tsze Ins. Ass'n*, 242 U.S. 430 (1917).

Similarly here, the questions now raised by the Government but not presented at the trial, do not find a basis in the Record actually made in this case, and should not be considered here in this case.

## II

THE STATUTORY LANGUAGE REQUIRES THE CONCLUSION REACHED BY THE COURTS BELOW THAT THE TAXPAYER IS ENTITLED TO COMPUTE ITS PERCENTAGE DEPLETION DEDUCTION ON THE SELLING PRICE OF THE BURNT CLAY PRODUCTS WHICH IT OBTAINED BY PROCESSING ITS FIRE CLAY AND SHALE.

Section 114(b)(4)(A)(i) and (iii) of the Internal Revenue Code of 1939 allowed the taxpayer a depletion

deduction of 5% of its "gross income from the property" in the case of its shale and 15% of its "gross income from the property" in the case of its fire clay, limited in each case to 50% of "the net income of the taxpayer (computed without allowance for depletion) from the property." Section 114(b)(4)(B) provides the definition of "gross income from the property" which applies in computing the taxpayer's percentage depletion deduction allowed by Section 114(b)(4)(A), and it is the meaning of this definition which is at issue in this case.

We agree with counsel for the Government (Br. 26-27) that the crucial language in this case is the following portion of the definition:

"As used in this paragraph the term 'gross income from the property' means the gross income from mining. The term 'mining' as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products . . . ."

However, in construing the statutory definition, which is set out in full in Appendix I (pp. 123-24 *infra*), all of the language should be considered and every effort should be made to interpret each portion of it in a reasonable way consistent with the reasonable meaning of other portions. In order to harmonize its restrictive interpretation of other language in the statute with the

key phrase, "commercially marketable mineral product or products," the Government is forced to give that term an artificial meaning which in effect writes it out of the statute. The Government asks the Court to substitute for "commercially marketable" the quite different term, "fit for commercial or industrial use." (Br. 18, 21, 25, 26, 76, 78, 80, 85, 90)

The meaning of "commercially marketable mineral product or products" is vitally important to interpretation of the statute in accordance with the Congressional intent. Although Government counsel stress the term "ordinary treatment processes," and refer to the words "normally applied... to obtain the commercially marketable mineral product" as "the dependent clause" (Br. 18, 90), the meaning of the statute must necessarily turn upon the meaning of "commercially marketable mineral product or products." This is so because the "ordinary treatment processes" included in the statutory definition of mining are those "normally applied by mine owners or operators *in order to obtain the commercially marketable mineral product or products.*"

**A. A "commercially marketable" product within the meaning of the statute is a product which can actually be sold commercially, as the courts below and many other courts have held, not merely a product "fit for commercial use" as contended by the Government.**

**1. The courts have properly interpreted "commercially marketable" in accordance with its ordinary meaning.**

In order for a product to be "commercially marketable" within the ordinary meaning of that term, there



must be an actual, continuing, regular opportunity to sell it on a practical business basis.

In all of the cases involving the meaning of "the commercially marketable mineral product or products," the courts have recognized that the opportunity to sell a negligible quantity of a product does not make it "commercially marketable."<sup>1</sup>

As the courts have also agreed, "commercially marketable" is not a hypothetical or theoretical term. The mere fact that a product is theoretically usable for a certain purpose does not make it "commercially marketable"; there must be an actual, existing opportunity to sell it. As the Tax Court has said, to hold that a product is "commercially marketable" on the basis of theoretical usability, regardless of whether in fact it can be sold, "is to read the words 'commercially marketable' out of the statute."<sup>2</sup>

If the qualifying word, "commercially," is to be given any meaning, in order for a product to be commercially marketable it must be possible to sell it on a practical business basis. Unless it is economically feasible to sell the product, it is not commercially marketable. In *Commissioner v. Iowa Limestone Co.*, 269 F.2d 398, 403 (8th Cir. 1959), the Court of Appeals concluded that "the profit-making aspect must be given

<sup>1</sup>E.g., *Dragon Cement Co. v. United States*, 244 F. 2d 513 (1st Cir. 1957), cert. denied, 355 U.S. 833 (1957); *United States v. Merry Bros. Brick and Tile Co.*, 242 F.2d 708 (5th Cir. 1957), cert. denied, 355 U.S. 824 (1957); *United States v. Sapulpa Brick and Tile Corp.*, 239 F.2d 694 (10th Cir. 1956); *United States v. Cherokee Brick & Tile Co.*, 218 F.2d 424 (5th Cir. 1955).

<sup>2</sup> *Riverton Lime and Stone Co.*, 28 T.C. 446, 452 (1957).

consideration in determining whether a mineral product is commercially marketable" and quoted with approval the following interpretation of "commercially marketable" in *Sperta Ceramic Co. v. United States*, 168 F. Supp. 401, 404 (N.D. Ohio 1958):<sup>3</sup>

"Taxpayer equates 'commercially marketable' with 'economically feasible', and adopts the view that before a product is commercially marketable there must be the prospect of substantial sales with the possibility of a profit being made thereby.

"The Government's theory on the definition of this term is that it means only salable or fit to be offered for sale in business intercourse.

"Both logic and the decided cases support the taxpayer's interpretation.

"Websters' New International Dictionary (2nd Ed.) defines 'commercial' as:

"1. Of or pertaining to commerce \* \* \*

"2. Having financial profit as the primary aim."

"'Marketable' is defined as:

"1. Fit to be offered for sale in a market; \* \* \*

"2. Wanted by purchasers, saleable; \* \* \*"

"Thus, 'marketable' can be said to be 'saleable, or fit to be offered for sale in a market', which is exactly the definition the Government wishes to ascribe to 'commercially marketable'. The fallacy of this desired interpretation is the failure to include the profit making aspect, 'commercial'."

<sup>3</sup> Now on appeal to the Sixth Circuit.

It is the concept of economic feasibility so expressed which the Court of Appeals had in mind in the instant case in holding that products (raw fire clay and shale) which the taxpayer "could not sell at a profit" were not commercially marketable. As the courts below recognized, a product is not commercially marketable unless a market for it is economically available. The Court of Appeals did not mean that an assured profit is essential to commercial marketability or, as the Government suggests (Br. 81), that Congress undertook by the depletion statute "to guarantee miners a profit."

In all of the cases which have arisen under this statute, the courts have treated "commercially marketable" as having its ordinary meaning and effect. As used in the statute, it refers to a product that can actually be sold on a commercial basis. So construed, as the court below said, its application is and has been treated by the courts as a question of fact. (R. 270)

**2. The Government's construction of "commercially marketable" is not a reasonable interpretation of the words used by Congress but an unwarranted substitution of quite different words.**

The Government gives some recognition to the ordinary meaning and effect of "commercially marketable" as a statutory standard by the following concession in its brief (p. 85):

"If the words 'commercially marketable mineral product' stood alone in the statute and one ignored the purpose, history and related language, there might be some basis for suggesting that 'commercially marketable' means 'marketable by the individual seller at a profit' . . ."

The Government then argues that the context of the phrase requires that it be interpreted as "the product fit for sale or commercial use." (Br. 85-86)

In essence the Government's argument as to the context of the phrase is that "ordinary treatment processes normally applied by mine owners or operators" must be interpreted as restricted to mining processes as distinguished from manufacturing processes. (Br. 7-9) \* For the Government, it is not enough that processes necessary to obtain a commercially marketable mineral product are the ordinary processes normally applied by miners; although the statute does not say so, the Government contends that the processes must be "normal for miners, *qua* miners." (Br. 7-8)

The Government's argument in this case is the same

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\* It was not until 1953, almost 10 years after the statutory definition of "gross income from the property" was enacted by Congress in 1943, that the Treasury adopted a regulation interpreting that definition as intended to exclude processes of a manufacturing nature even though they are applied and required in order to obtain a commercially marketable mineral product. This regulation, added to Section 29.23(m)-1(f) of Treasury Regulation 111 by T.D. 6031, 1953-2 CUM. BULL. 120, is the italicized portion of that Section as reprinted in Appendix I, pp. 125-28 *infra*. In cases in which the Government has relied upon this regulation, it has been held invalid on the ground that the statutory definition of "gross income from mining" does not permit such an interpretation. *E.g.*, *Dragon Cement Co. v. United States*, 244 F.2d 513, 518, 520 (1st Cir. 1957), *cert. denied*, 355 U.S. 833 (1957); *Cherokee Brick & Tile Co. v. United States*, 122 F. Supp. 59, 63-64 (M.D. Ga. 1954), *aff'd*, 218 F. 2d 424 (5th Cir. 1955); *Sapulpa Brick and Tile Corp. v. United States*, 56-2 U.S.T.C. ¶ 9709 (N.D. Okla. 1956), *aff'd*, 239 F.2d 694 (10th Cir. 1956).

The Government's brief in this case makes no mention of the 1953 regulation, although it was the basis for the Revenue Service's computation of the taxpayer's percentage depletion deduction for the taxable year involved. R. 95-96, 110-11; see Rev. Rul. 54-109, 1954-1 CUM. BULL. 62 (Resp. App. II, p. 16f).

argument in substance which it made in the *Dragon Cement Company* case and the *Merry Brothers Brick and Tile Company* line of cases,<sup>5</sup> in which it unsuccessfully petitioned this Court for a writ of certiorari to review decisions holding that the statutory definition of mining includes *all* "ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products," even though such processes may be in the nature of manufacturing. In its petition for certiorari in the *Merry Brothers* group of cases (p. 16), the Government made its argument directly, as follows:

"... Congress was primarily concerned not with the marketability of the mineral product, but with the nature of the processes which were to be considered 'mining' processes."

The Government insisted in its petition for certiorari in this case (p. 12) that the issue in *Merry Brothers* was "entirely distinct" from the issue presented in this case. In *Merry Brothers*, it was contended, the issue was what is included in the phrase "ordinary treatment processes," whereas the issue presented in this case is how to determine the identity of the "commercially marketable mineral product." Now, however, it states frankly in its brief (pp. 18-19, 88-91) that the issue in this case and the issue decided in *Merry Brothers* are "closely related," and it squarely attacks the legal approach adopted by the courts in *Merry Brothers* and like cases as erroneous. Having been unsuccessful in its previous attempts to persuade the courts to ignore

<sup>5</sup> See note 1, p. 43 *supra*.



completely the commercially marketable products rule, however, it now urges that the same result should be achieved by construing "commercially marketable" to mean "fit for commercial or industrial use." (Br. 18)

Under the construction of the statute which the Government finds it necessary to urge in support of its position in this case, a product might be considered "commercially marketable" even though it is not sold and could not be sold by any miner anywhere. In this respect, the Government has changed its theory somewhat from that stated in its petition for certiorari in this case. In the petition (pp. 14-15), it took the position that the "commercially marketable mineral product" is the basic (least processed) product *sold* by the particular branch of the mining industry. Now, however, it takes the position that the "commercially marketable mineral product" is the "basic mineral product fit for commercial use." (*E.g.*, Br. 26) "Sales are significant for purposes of applying the statute," it repeats in its brief (pp. 18, 85), "not because an ability to sell profitably is relevant, but only because sales may provide conclusive proof that a mineral product has reached a state where it is fit for commercial or industrial use—proof, in other words, that the mineral has passed beyond the point where it can be said to be undergoing the ordinary processes of 'mining.'" Obviously, the Government considers that other proof will suffice in the absence of sales; the Commissioner merely determines what processes he considers are mining—"those processes which a non-integrated miner would have to use." (Br. 87) In the Government's view, those processes make the mineral product "com-

mercially marketable" whether or not it can then be sold by the particular miner or any other miner, because it is then "fit for commercial or industrial use."

No language in the statutory definition of "mining" requires the utter disregard of "commercially marketable" for which the Government contends. Indeed, it would be strange to find any support for such a result in a definition which Congress placed in the statute "to make certain that the ordinary treatment processes which a mine operator would normally apply to obtain a marketable product should be considered as a part of the mining operation . . . ."<sup>6</sup>

The Government asks this Court to substitute for "commercially marketable"—the carefully chosen words which Congress deliberately used for a clearly stated purpose—some quite different words which would not accomplish that purpose. In support of its argument that Congress meant "fit for commercial or industrial use" when it said "commercially marketable," the Government relies upon the term "ordinary treatment processes" and upon the listing in the statute of certain processes which that term shall include in the case of specified ores and minerals, and of certain processes which it shall not include in the case of specified ores. The Government does not contend that fire clay and shale are included among the minerals for which

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<sup>6</sup>S. REP. NO. 627, 78th Cong. 1st Sess. 23 (1943) (Gov't App. B., p. 210).

included or excluded processes are listed. In fact, it concedes that they are not. (Br. 6, 21) Moreover, the Government concedes that the listing of included processes is not "necessarily" all-inclusive even with respect to the listed minerals. (Br. 31 n.21) However, it argues that the term "ordinary treatment processes" itself and the types of processes listed show that the treatment processes which are included within the statutory definition of "mining" are of a "definite and restricted kind" (Br. 34), which is the *same* for all classes of mines and minerals. This argument by the Government, based on its assignment of "particularized and technical meanings" to the terminology used in the statute (Br. 34) and on an attempted technical classification of the types of treatment processes listed in the statute, is unsound. There is no indication from the statutory language or legislative history that Congress contemplated that resort to such technical theories should be necessary to discover its intention in defining "gross income from the property." Furthermore, the Government's theories are unsound on a technical basis, as shown by the analysis and references

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<sup>7</sup> This concession is required. Section 3797(b) of the Internal Revenue Code of 1939 provides:

"The terms 'includes' and 'including' when used in a definition contained in this title shall not be deemed to exclude other things otherwise within the meaning of the term defined."

This section was referred to by the courts in *Townsend v. The Hitchcock Corp.*, 232 F.2d 444, 447 (4th Cir. 1956) and *Deacon Cement Co. v. United States*, 244 F.2d 513, 516 (1st Cir. 1957), cert. denied, 355 U.S. 833 (1957), in concluding that the enumeration of processes in the statute is in no way exclusive even as to the ores and minerals covered.

to technical authorities which we have set out in Part A of our separately bound Appendix 41 (p. 1) and will summarize here.

The Government argues that the "statutory scheme," both in its use of the phrase "ordinary treatment processes" and in its listing of particular processes "which satisfy that concept," is in "full accord" with "the mining industry's own view of the scope of mining," as expressed in technical treatises and trade journals. (Br. 8, 31) In this technical literature, says the Government, mining "is regarded as including certain ordinary preparatory processes employed after extraction of the mineral to separate the valuable constituent of the natural deposit from waste matter." (Br. 8-9, 31) Of course, to say that certain processes are regarded by the industry as included in mining is not to say that other processes essential to obtaining a marketable product are *not* so regarded by the industry. Trying to bridge this gap, the Government suggests (Br. 31-33, 86) that in the industry "treatment processes" means the same thing as "mineral dressing," a technical term which does relate to the separation of the valuable constituent from waste.

This attempted restriction of the intended meaning of "ordinary treatment processes" is unwarranted. In the first place, there is no basis for the Government's suggestion that in the mining industry "treatment" is merely a synonym for "mineral dressing." (Resp. App. 11, pp. 1-2) \* In the second place, the processes

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\* Indeed, the leading authority in the field of mineral dressing, relied upon in the Government's Brief for its statement as to the meaning of "treatment" and other points, obviously does not con-

specifically listed in the statute as included in "ordinary treatment processes" include processes which do not involve separating the valuable constituent from waste matter. (Resp. App. II, pp. 2-3) The Government recognizes that the listing of such processes as "ordinary treatment processes" necessarily refutes any contention that Congress intended to restrict the term to mineral dressing involving separation of the valuable constituent from waste matter. Conceding that putting minerals in "shipping grade or form may require, in some instances, such preparatory processes as crushing, screening, or drying" (Gov't Br. 9, 33), the Government shifts to another classification theory.

This ultimate attempt by the Government to restrict the meaning of "ordinary treatment processes" by classification of the included processes listed in the statute is on the basis of a distinction between mining processes, which it says "do not destroy the physical and chemical identity of the minerals" (Br. 9), and manufacturing processes, which it says "involve the mechanical or chemical transformation of inorganic and organic substances into new products." (Br. 9) This attempted classification is also refuted by the processes listed in the statute as included in "ordinary treatment processes." Many of these processes involve changes in the physical or chemical identity of the material or both. (Resp. App. II, pp. 3-6)

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fine the term "treatment" to mineral dressing. In fact, he includes a description of the processing of common clay and fire clay into brick and tile under the heading "Treatment" in his discussion of "Clay." TAGGART, HANDBOOK OF MINERAL DRESSING, 3-13 through 3-15 (1945 ed.) (Resp. App. II, p. 170).



It is apparent from the language of the statute—both the definition of “mining” as including “the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products” and the specification of processes included in and excluded from the term “ordinary treatment processes” for various kinds of minerals and ores (Resp. App. II, pp. 6-8)—that Congress was not trying to draw a line between mining and manufacturing based on the technical nature of the processes, and whether they would be classified as mining processes or manufacturing processes by experts, who are bound to disagree. Rather, Congress was concerned with the practical test of a commercially marketable mineral product and defined “mining” as including *all* “the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products.”

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The Government's argument that the language of the statutory definition of “mining” shows a Congressional intent to exclude processes which might be classified technically as manufacturing, even though they are required in order to obtain a product for which there is actually a commercial market, has been advanced in numerous other cases. The argument has been rejected in all those cases by the courts, including four Courts of Appeals, all of which held that “commercially marketable” must be interpreted in accord-

ance with its ordinary meaning.<sup>9</sup> The carefully considered opinion rejecting the Government's argument in *Dragon Cement Co. v. United States*, 244 F.2d 513 (1st Cir. 1957), *cert. denied*, 355 U.S. 833 (1957), is set out in Respondent's Appendix II (p. 11). In that opinion, Judge Magruder stated that the Court was unable to perceive any ambiguity in the phrase, "commercially marketable mineral product or products," and observed that three other Courts of Appeals which had weighed the same arguments by the Government and construed this "critical statutory phrase" had held it to be "clear and unambiguous" in favor of the taxpayer's interpretation. (Resp. App. II, p. 23).

The statutory definition of "mining" would be meaningless and useless if it were construed as the Government asks. The Government contends that "commercially marketable mineral product or products" as used

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<sup>9</sup> *United States v. Cherokee Brick & Tile Co.*, 218 F.2d 424 (5th Cir. 1955) (brick and tile clay); *Townsend v. The Hitchcock Corp.*, 232 F.2d 444 (4th Cir. 1956) (talc); *United States v. Sapapa Brick and Tile Corp.*, 239 F.2d 694 (10th Cir. 1956) (brick and tile clay); *Dragon Cement Co. v. United States*, 244 F.2d 513 (1st Cir. 1957), *cert. denied*, 355 U.S. 833 (1957) (cement rock); *United States v. Merry Bros. Brick and Tile Co.*, 242 F.2d 708 (5th Cir. 1957), *cert. denied*, 355 U.S. 824 (1957) (brick and tile clay).

"Commercially marketable" has also been interpreted in accordance with its ordinary meaning by two other Courts of Appeals to which the Government made a somewhat different argument—i.e., the Courts of Appeals for the Seventh Circuit, in the instant case, and the Eighth Circuit, in *Commissioner v. Iowa Limestone Co.*, 269 F.2d 398 (8th Cir. 1959) (limestone). See also *New Idria Quick-silver Mining Co. v. Commissioner*, 144 F.2d 918 (9th Cir. 1944), discussed in Kent, *The New Idria Decision*, 30 MINING CONGRESS JOURNAL 24 (1944) (Gov't App. B, pp. 479-81).

in the statute refers to a mineral product which has reached "a state where it is fit for commercial or industrial use"; and the Government considers that such a state is reached once "the mineral has passed beyond the point where it can be said to be undergoing the ordinary processes of 'mining.'" (Br. 85)

If that were so, the statutory definition could be re-written correctly as follows:

The term "mining" as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain a mineral which has undergone the ordinary processes of "mining."

Or, in other words, "mining" shall be considered to include what the Commissioner considers "mining."

If the Government's interpretation were adopted, the special definition of "mining" which Congress placed in the statute would be rendered nugatory. The scope of "mining" under the statute would be left completely to regulation by the Treasury. This, of course, is the result greatly desired by the Treasury, which urged Congress not to add the definition to the statute in the first place on the ground that the subject should be covered by Treasury regulations.<sup>10</sup>

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<sup>10</sup> Senate Debate, 1942, 88 CONG. REC. 8033 (Gov't App. B, pp. 196-97).

**B. The "commercially marketable mineral product or products" means the first product or products actually obtained from a mineral by the miner which he has an opportunity to sell on a commercial basis.**

The wording and structure of the statute and the nature of the determination of commercial marketability required by the statute show that "the commercially marketable mineral product or products" refers to the first product or products actually obtained by the taxpayer in his processing of his mineral which he has an opportunity to sell on a commercial basis.

Section 114(b)(4)(A) provides that the depletion allowance, in the case of designated mines and other natural deposits, shall be a specified percentage "of the gross income from the property during the taxable year." As applied to this case, "gross income from the property" obviously refers to this particular taxpayer's "gross income from the property," and "the property" is the mine operated by this taxpayer.

Section 114(b)(4)(B) provides that "gross income from the property" means "the gross income from mining." As applied here, this refers to this taxpayer's gross income from its "mining" operations, which are defined specially to include not merely the extraction by the taxpayer of its fire clay and shale from the ground but also certain processes applied by the taxpayer in order to obtain "the commercially marketable mineral product or products."

The statutory definition of "mining" was provided for the purpose of computing the "gross income from the property" of individual taxpayers, and in applying it to compute the gross income from the property of a

particular taxpayer, it is necessary to determine first the identity of "the commercially marketable mineral product or products" in his case. The natural and ordinary way to apply this tax statute to a particular taxpayer is to determine what product or products the taxpayer first obtains in his line of processing of the mineral from his mine which he has an opportunity to sell on a commercial basis.

In contending that Congress has imposed an "industry-wide test" for the commercially marketable product (Gov't Br. 7, 27), the Government apparently relies upon the use of the terms "ordinary" and "normally" and the plural reference to "mine owners or operators." To be sure, these statutory terms impose restrictions, in that the treatment processes applied by the taxpayer to obtain the product or products which are his "commercially marketable mineral product or products" must be the ordinary treatment processes normally applied by mine owners or operators in order to obtain such product or products. In order to determine whether these restrictive provisions are met, reference must be made to the practices of other miners in obtaining such product or products. But this does not mean that Congress intended that a taxpayer's gross income from *his* property should be determined on the basis of the first commercially marketable product obtained by some other miner or miners of the same mineral. The taxpayer's gross income from the property must be determined on the basis of processes which he actually applies to obtain a product which he can market commercially, with the restriction that they must



be the ordinary processes normally applied by miners in order to obtain that product.

The Government argues that the statute does not permit each taxpayer to "include such processes as he may use in order to obtain the particular product which he markets." (Br. 27) We do not contend that the statute makes the selling price of any product a taxpayer may choose to sell the base for percentage depletion. As the Court below recognized (R. 273), the statute does not permit a taxpayer to compute percentage depletion on the selling price of a product processed beyond the stage at which it becomes commercially marketable. That is what the courts have meant in stating that the statute limits the depletion base to the *first* "commercially marketable mineral product." They have not meant that the statute contemplates a single "basic mineral product" for each "branch of the mining industry," as the Government would interpret it. (Br. 26, 76) Thus, in *United States v. Cherokee Brick & Tile Co.*, 218 F.2d 424, 425 (5th Cir. 1955), the court referred to "the commercially marketable mineral product" as "the first product which is marketable in commerce," but it allowed computation of percentage depletion for the taxpayer's brick and tile clay on the selling price of both the burnt brick and the burnt tile which the taxpayer produced from the clay.<sup>11</sup> In the case of each product, it was the first product obtained in the particular line of processing which was commercially marketable. This does not mean that under the view of the Courts of Appeals in

<sup>11</sup> See also cases discussed pp. 64-67 *infra*.

this and other cases "the possibilities for depletion allowances are virtually limitless," as the Government argues. (Br. 23) The same fear was expressed by the Government in *Commissioner v. Iowa Limestone Co.*, 269 F.2d 398 (8th Cir. 1959) and was answered by the court as follows (p. 405, Resp. App. II, p. 42):

"The Commissioner expresses some fear that the logical result of the Tax Court's holding is that a miner can use as his depletion base the gross sale price of any product he chooses to manufacture. Such fear is without foundation. The depletion statute as interpreted by the Tax Court limits the depletion allowance to the first commercially marketable chemical grade limestone produced. . . . For depletion purposes the product may not be processed beyond the stage where it becomes a commercially marketable product. . . ."

The plural reference to "products" in the phrase, "the commercially marketable mineral product or products," shows that Congress did not intend to establish arbitrarily a single "basic product" for each mineral named in the statute. The Government claims that the plural reference to products is not inconsistent with its reading of the statute. (Br. 27) However, the Government's own explanation of Congress' use of the plural is inconsistent with its theory of interpretation. It describes the use of "products" as "merely a recognition of the fact that one mining operation (as in this case) may yield more than one mineral product (here the clay and shale)." (Br. 27) Thus, the Government

has resorted to an explanation which inherently concedes that the statutory phrase, "the commercially marketable mineral product or products," refers to the "product or products" of a particular mining operation, not to a single, industry-wide "basic product" of the particular mineral. If Congress had used the phrase to refer to the basic product of each mineral on an industry-wide basis, there would have been no need to use the plural. There would be only one "commercially marketable mineral product" of fire clay and only one "commercially marketable mineral product" of shale, and the statute would be read separately for each.

It seems inconceivable that Congress would have used the plural reference to "products" for the reason suggested by the Government if its intention had been to fix "for each mineral an ascertainable and uniform cut-off point binding upon all miners" of that mineral. (Gov't Br. 9, 34) If that had been the intention of Congress, surely it would have avoided the use of a plural term which was unnecessary and which was inconsistent with that purpose.

The Government's explanation of the plural reference to products is not only inconsistent with its own theory but also attributes to Congress' use of the plural a limited and rather technical meaning which is out of harmony with the general language of the statutory definition.<sup>12</sup>

<sup>12</sup> In attempting to support its explanation of the plural reference to products, the Government points out (Br. 27-28) that "a single ore frequently contains many different metals," and that this is

Further evidence of the Congressional intent is found in its choice of the words, "commercially marketable." The question of commercial marketability is not one which can be determined satisfactorily on an industry-wide basis for each class of minerals covered by the statute. Congress has undertaken to determine itself the stage at which certain ores become commercially marketable when treated by certain methods by specifying in the statute that the term "ordinary treatment processes" shall not include in the case of such ores "electrolytic deposition, roasting, thermal or electric smelting, or refining."<sup>13</sup> However, as Congress has recognized by *not* designating excluded processes for other classes of minerals, the question simply cannot always be determined satisfactorily on an industry-wide basis. In the case of many classes of minerals, including fire clay and shale, the first commercially marketable product will vary from area to area, or according to the grade of the mineral or the type of

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reflected in clause (iv) of Section 114(b)(4)(B), which refers to the "processes used in the separation or extraction of the product or products from the ore." As we shall show (pp. 62-63 *infra*; and Appendix II, pp. 10-11), the processes included by clause (iv) in "ordinary treatment processes" and those excluded from that term, show that Congress contemplated that there would be different commercially marketable products of ore processed for the same metal, depending upon the method used. Therefore, the plural reference to "products" in clause (iv) does not necessarily have the narrow meaning suggested by the Government.

<sup>13</sup> As the Government's brief states (p. 8), in the case of metallic ores, Congress "has excluded smelting and refining—processes which take place after the ore concentrate (saleable at that stage, to smelters) has been obtained." See also Resp. App. II, pp. 6-8.

mine or the line of processing used. This is not to say that the question will be determined differently for every miner of a particular mineral. There is nothing peculiar or unique, for instance, about the mining of fire clay from an underground mine or at a distance from any markets for the raw fire clay and shale, which are the circumstances in this case which precluded the taxpayer from marketing the raw products on a commercial basis.<sup>14</sup>

Congress' recognition that "the commercially marketable mineral product or products" within the meaning of the statute may be different for miners of the same mineral is shown by the nature of certain processes which it has expressly listed in the statute as included in or excluded from "ordinary treatment processes." As shown in Part A of Respondent's Appendix II, certain processes included as "ordinary treatment processes" in the case of coal are applied to substantial amounts of coal in order to make it marketable but are not applied before sale to other substantial amounts of coal. (Resp. App. II, pp. 8-9). Furthermore, the statute expressly includes as "ordinary treatment processes" certain metallurgical processes yielding metallic gold or metallic copper, which are different and more processed products than the ore concentrate. Yet the ore concentrate is the commercially marketable product in the case of gold ore

<sup>14</sup> See, e.g., *Standard Clay Mfg. Co. v. United States*, 176 F. Supp. 590 (W.D. Pa. 1959), now on appeal to the Court of Appeals for the Third Circuit.



or copper ore which is smelted, as Congress recognized in excluding smelting from "ordinary treatment processes." (Resp. App. II, pp. 10-11)

The courts have also recognized that "the commercially marketable mineral product or products" within the meaning of the statute may be different for miners of the same mineral. In applying the statute to various factual situations in the complex field of mining, the courts have had to deal with the geologic fact that there are different grades of the same mineral and with the economic fact that the market situation for mineral products varies. They have recognized that the determination of "the commercially marketable mineral product or products" under a proper interpretation of the statute must be made on the basis of such facts and that there is not necessarily a single commercially marketable product for each class of mineral listed in the statute. They have considered this a necessary conclusion in order to carry out the Congressional purpose expressed in the phrase, "commercially marketable mineral product or products."

The viewpoint of the courts which have considered the matter was expressed by the Court of Appeals in its opinion in this case (R. 271) as follows:

"We are unable to accept the theory that a taxpayer's depletion allowance is to be computed on the basis of a representative market or field price for a product which taxpayer could not sell at a profit. To do so would be to deprive of all meaning the words 'commercially marketable' as used in the Code provision here considered."

In *Townsend v. The Hitchcock Corp.*, 232 F. 2d 444 (4th Cir. 1956), the tale mined by the taxpayer was subjected to two distinct and separate processes. That which was suitable for the purpose was cut into crayons; the rest was pulverized. The pulverized tale was sold at a price which was only a small fraction of the selling price of the tale crayons. The trial court found that there was no commercial market for the tale until it was pulverized or cut into crayons, and that there were no sales of tale in its crude form as it comes from the mine anywhere in the United States except for a small percentage of the national output sold by itinerant miners on the West Coast. The Government argued that none of the processes applied by the taxpayer after extraction of the tale were includible in "mining." The Court of Appeals for the Fourth Circuit held that the taxpayer had two commercially marketable products, the pulverized tale and the tale crayons, and that the applicable percentage should be applied to the selling price of each product to compute the taxpayer's depletion deduction under Section 114 (b) (4) of the Internal Revenue Code of 1939.<sup>15</sup>

In *Commissioner v. Iowa Limestone Co.*,<sup>16</sup> the taxpayer quarried a relatively rare type of limestone suit-

<sup>15</sup> For details as to the processing and relative value of the two products, see the record appendix to the Brief for Appellant, pp. 62, 115-16, 140, 184-87. *Townsend v. The Hitchcock Corp.*, 232 F. 2d 444 (4th Cir. 1956). In *International Tale Co.*, 15 T.C. 981 (1950), the Tax Court reached the same result as to pulverized tale, the only product processed by the taxpayer in that case.

<sup>16</sup> 269 F.2d 398 (8th Cir. 1959), affirming, 28 T.C. 881 (1957). The opinion of the Court of Appeals is set out in Respondent's Appendix II, p. 28.

able for chemical use. It processed the stone by crushing and grinding it into a finely pulverized form, in which it was sold to feed and minerals manufacturers for approximately \$9.00 per ton. These purchasers required that the stone be finely ground and that it meet rigid specifications as to chemical composition. The Commissioner contended that the first commercially marketable product of limestone, regardless of grade, is crushed limestone as sold for road or agricultural purposes for prices ranging from \$1.35 to \$1.75 per ton. Although the taxpayer's plant as constructed did not produce limestone satisfactorily crushed for road or agricultural purposes, it could have been converted to do such crushing. The Court of Appeals for the Eighth Circuit refused to accept the theory that there is a single commercially marketable product for all limestone, reasoning that "the profit-making aspect must be given consideration in determining whether a mineral product is commercially marketable," that the taxpayer "had the right to market its chemical grade limestone for the purpose for which it was most suited and in a field where it would command a fair price," and that it "was not economically feasible for the taxpayer to market its superior stone as ordinary road rock."<sup>17</sup>

Holding that the company's commercially marketable product was the pulverized chemical grade limestone which it sold, the court quoted with approval the Seventh Circuit's opinion in the instant case that Congress did not intend "that the depletion allowance for each mineral be reduced to the common denominator

represented by a conceivable product most cheaply produced from each mineral."<sup>18</sup>

As in this case, the Government argued in the *Iowa Limestone* case that its single-product theory was necessary in order to avoid discrimination. The court's comment on this argument was as follows:

"The Commissioner also argues that to give the taxpayer a greater depletion base than owners of inferior limestone quarries would be inequitable. At least as good an argument can be made that it would be unfair to the taxpayer not to allow it depletion based upon the reasonable consideration of the value of its depletable product. However, such arguments have no weight either way as the depletion base is controlled entirely by the statute. Any inequities call for legislative rather than judicial action."<sup>19</sup>

In *Albin C. Halquist*,<sup>20</sup> the Tax Court considered a similar question and reached the same result. The taxpayer in that case quarried dolomite, some of which it processed into dimension building stone and some of which it crushed for use as aggregate in construction and as agricultural stone. The stone sold as crushed stone came from a ledge which was not suitable for

<sup>18</sup> 269 F.2d at 404 (Resp. App. II, p. 39). The Eighth Circuit has since followed the same reasoning in another case involving chemical grade limestone. *Bookwalter v. Centropolis Crusher Co.*, 272 F.2d 391 (8th Cir. 1959).

<sup>19</sup> 269 F.2d at 405 (Resp. App. II, p. 42).

<sup>20</sup> 33 T.C. 304 (1959). The opinion is reproduced in Respondent's Appendix II, p. 44.

dimension stone and from waste in the processing of dimension stone. The Commissioner contended that the single commercially marketable product for the dolomite and limestone industry is crushed stone, the crudest, least processed product marketed in more than negligible quantities, and that the taxpayer's depletion base for the stone processed into building stone was limited to the income that would have been derived if such stone had been sold as crushed stone. The Tax Court rejected this theory and held that the taxpayer was entitled to compute his percentage depletion allowance on the selling price of each of his products.

In addition to these decisions, the Tax Court in other cases and numerous District Courts have concluded, in applying the statute to various minerals in differing and complex factual situations, that Congress intended to provide flexibility in the determination of the commercially marketable products in accordance with the facts of the situation, and did not intend to have the question decided arbitrarily on an industry-wide basis.<sup>21</sup>

**C. The first products obtained by the taxpayer which it had an opportunity to sell on a commercial basis were the burnt clay products which it sold.**

The Government does not challenge the District Court's finding (Fdg. 12, R. 5), endorsed by the Court of Appeals as supported by the record (R. 267), that there was no market in which the taxpayer could have sold its fire clay and shale at a profit before it was proc-

<sup>21</sup> See chart of cases in Part E of Respondent's Appendix II, pp. 173-81.



essed into sewer pipe and other burnt clay products. (Br. 6, 21). However, by stating that this was due to the taxpayer's "high" mining and transportation costs (Br. 2, 6), without further explanation except a reference to its "strategic market location" as "poor"

(Br. 84), the Government's brief may create the impression that the taxpayer's inability to sell raw fire clay and shale profitably was due to inefficient mining operations and poor selection of a mine location. There is no basis for such an inference. The taxpayer operated an underground mine but there is nothing to indicate that its mining costs were any higher than other similar operations. The Court of Appeals stated that the record showed that there existed in Indiana in 1951 a substantial market for fire clay and shale, but that "it is also apparent from the record that taxpayer could not have sold its fire clay and shale in that market *at a profit* because of prohibitively high mining and transportation costs." (R. 267). It is obvious from the court's discussion of the facts later in its opinion that it meant that the taxpayer's mining and transportation costs were prohibitively high in relation to those of the strip miners who supplied that market, so that the taxpayer had no access to it. The court noted that the market for fire clay and shale in Indiana existed primarily in a limited area near Brazil, Indiana (R. 271-72), which is located 140 miles from the taxpayer's mine at Cannelton. (R. 44)

The reason why the Brazil miners were able to sell clay and shale at prices below the taxpayer's mining costs was explained by the Court of Appeals as follows (R. 271):

"Those companies selling fire clay in Indiana concerning which the Government introduced evidence fall into two categories. There are those operators who engage primarily in strip mining of coal and, who, during their operations, strip bare so-called underclay which they sell as a by-product. Secondly, there are those which mine underclay which has already been laid bare by previous strip mining operations. The mining costs of such operators would be considerably below those of taxpayer which operated an underground mine." <sup>22</sup>

With regard to the location of the taxpayer's mine, the record shows that the clay in the taxpayer's mine was the best for making sewer pipe mined in Indiana

<sup>22</sup> A footnote in the Government's brief (p. 83 n.83) states that a miner located in Kentucky, directly across the river from taxpayer, sold substantial quantities of both fire clay and shale to a sewer pipe manufacturer. (See also Gov't Br. 22) This is not an accurate statement. The "miner" referred to, L. R. Chapman, did not sell fire clay and shale. He operated a coal mining, farming and contracting business and dug ponds, built roads, and did earth movement work on a contract basis. (R. 163, 180-81) In 1951, Chapman mined and delivered clay and shale to the Owensboro Sewer Pipe Company at Owensboro, Kentucky, from a five acre tract of land which he had previously sold to that company for \$50.00. (R. 168, 171-72) Chapman sold coal to Owensboro (R. 169, 245-46), and he had a contract to mine and deliver clay and shale for Owensboro at a rate of \$1.40 per ton for his services. (R. 168-72) In later years, Chapman mined and hauled clay and shale for several companies under similar arrangements. (R. 173-79) In all cases the prospecting and investigation of the properties in search of suitable clay and shale and the development and preparation of mining sites were done by the companies or at their direction and expense, with the understanding that Chapman would sell or lease the land to them if desired and would have a contract to mine and haul the clay for them. (R. 180, 185)

and that the Cannelton sewer pipe was the best produced in Indiana. (R. 127) Thus the location and mining costs which excluded the taxpayer's fire clay and shale from a market were not due to inefficiency. They were essential to obtain a particularly desirable clay, but they made a market for the raw minerals economically unavailable. The encouragement of discovery and exploitation of natural resources is inherent in a concept of depletion which is not limited to a return of cost,<sup>23</sup> and it certainly is not inconsistent with the Congressional purpose in adopting percentage depletion to encourage a miner to develop a superior deposit of fire clay and shale rather than to develop a poorer deposit merely because its location and situation are such that the crudest form of mineral product may be sold profitably. Nor is it inconsistent with the Congressional purpose for the taxpayer to be entitled to a larger depletion allowance for its fire clay and shale than the coal strip miner at Brazil who mined and sold clay as a by-product.

On the facts as found by the District Court, the first products actually obtained by the taxpayer which it could sell on a commercial basis were the sewer pipe and other burnt clay products which it sold. This finding was approved by the Court of Appeals and is not challenged by the Government.

The District Court also found that all of the processes applied by the taxpayer were the processes "normally applied by mine owners or operators" to obtain such products. (Edg. 10, R. 5) This finding has not

<sup>23</sup> See pp. 77-78 *infra*; Gov't Br. 37-38; *Dragon Cement Co. v. United States*, 244 F.2d 513, 514 (1st Cir. 1957), *cert. denied*, 355 U.S. 833 (1957) (Resp. App. II, pp. 11, 13).

been challenged by the Government either in the Court of Appeals (R. 272, 273) or here.

Therefore, the taxpayer is entitled to compute its deduction for depletion of its deposits of fire clay and shale on the basis of the selling price of the burnt clay products which were its commercially marketable mineral products.

**D. Even if the "commercially marketable mineral product or products" are to be determined on an industry-wide basis, the judgment should be affirmed since miners of fire clay and shale normally are required to process such minerals into burnt clay products to make them commercially marketable.**

We have shown that the Court below and all the other courts which have considered the question have correctly held that the statute must be applied by first determining the "commercially marketable mineral product or products" of the particular taxpayer and that "mining" then includes the processes which that taxpayer actually applies and which are the processes "normally applied by mine owners or operators" to obtain such product or products. However, even if this Court should accept the Government's contention (Br. 7) that "Congress has adopted a generic or class description—one which imposes an industry-wide test" which is "applicable to each class of mines" (Br. 27), still it does not mean that the Government should prevail in this case involving a producer of fire clay and shale.

If Congress has established an "industry-wide" test, then "mining" includes the processes which members of that "industry" (i.e., producers of that mineral ac-

cording to the Government, Br. 25) *normally* apply to obtain their commercially marketable product or products. What they "normally" do must be what they do *usually* and *ordinarily*. Thus "mining" would include the processes which producers of fire clay and producers of shale normally, usually, and ordinarily apply to obtain their commercially marketable products.

Because (as shown above, pp. 28-40), the Government agreed with taxpayer in the District Court that the issue was whether the *taxpayer's* clay was commercially marketable, there is no evidence in the record to show what processes producers of fire clay and of shale in the country as a whole "normally" apply to obtain their commercially marketable products.<sup>24</sup>

The record does show, however, as the Court of Appeals found (R. 272), that in Indiana, where taxpayer is located, "the integrated miner-manufacturer was the rule rather than the exception" in 1951.

Furthermore, the fact is that producers of fire clay and of shale in the country as a whole *normally* must put their clay in the form of burnt clay products (such as sewer pipe) in order to obtain their commercially marketable products, as shown by the findings of fact in other cases, where the Government *did* raise this issue in the District Court and where evidence on it *was* introduced. Thus, the findings in one such case show that more than 75% of the refractory and fire clay extracted from the ground must be put in the form

<sup>24</sup> In fact, the Pre-Trial Order, which the Government as well as the taxpayer approved, specifically limited the issue to be tried and precluded the introduction of any evidence on this point (pp. 37-38 *supra*).



of burnt clay products before it can be sold; that 90% of the producers of refractory and fire clay are required to put their clay in the form of burnt clay products in order to be able to sell such clay; and that:

“Both in plaintiff’s market area and in the United States as a whole, refractory and fire clay mine owners and operators normally are required to put their refractory and fire clay in the form of burnt clay products in order to obtain products which are commercially marketable.”<sup>25</sup>

The Government in its brief (p. 82) quotes statistics (which are not in the Record) from the Minerals Yearbook of the Bureau of Mines to show the sales of fire clay in 1951. However, these figures do not show that producers of fire clay normally sell their raw clay. In fact, they support the findings in the *Elgin-Butler* and *Acme* cases.<sup>26</sup> Thus, they show that, in 1951, 73%

<sup>25</sup> *Elgin-Butler Brick Co. v. United States*, 146 F. Supp. 378, 382 (W.D. Tex. 1956), *aff’d by stipulation*, 57-1 U.S.T.C. ¶9619 (5th Cir. 1957), *cert. denied*, 355 U.S. 824 (1957). Findings to the same effect were also made in *Acme Brick Co. v. United States*, 167 F. Supp. 911, 914 (N.D. Tex. 1956), *aff’d by stipulation*, 57-1 U.S.T.C. ¶9617 (5th Cir. 1957), *cert. denied*, 355 U.S. 824 (1957); *Acme Brick Co. v. United States*, 160 F. Supp. 604, 607 (N.D. Tex. 1957).

<sup>26</sup> It should be noted, however, that these figures published by the Bureau of Mines, although they are the only published statistics, do not give an entirely accurate or reliable report of the production and sales of fire clay and shale. For example, statistics as to each of these types of clay are lumped with statistics as to other types as well. Also, the Bureau of Mines relies on reports from producers, as compiled by state agencies, in preparing them, without checking the classification of the mineral (R. 136-37); thus, one producer may report that his clay is fire clay, whereas another producer with the same type of clay may classify his clay differently. Cf. R. 83.

of the fire clay and stoneware clay combined mined in the country was used by the producer rather than sold by the producer.<sup>27</sup>

With respect to shale, the figures on which the Government relies (Br. 83) show that even a greater percentage of the production is processed by the producer before being sold. Thus, the Minerals Yearbook for 1951 shows that 96% of the "miscellaneous clays, including shale and slip clay" produced was used by the producer in his own operations.<sup>28</sup>

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<sup>27</sup> U. S. BUREAU OF MINES, DEPT OF INTERIOR, 1951 MINERALS YEARBOOK 294.

The Government also quotes (Br. 82) statistics compiled by the Census Bureau for 1954 purporting to show that over 4,400,000 tons were "shipped by miners" and that "a little less than 4,000,000 tons were mined and used" by producers of burnt clay products. These statistics show nothing as to sales of fire clay. First, these figures include diaspore, as well as fire clay and stoneware clay. Furthermore, the tonnage shown as "mined and used" includes only clay mined and used where the mine and processing plant are part of the same "establishment" i.e., "a single physical location where mineral operations are conducted." The tonnage shown as "shipped by miners" therefore includes all tonnage shipped from the "mining establishment," including shipments by "mining establishments operated entirely to serve other establishments of the same company." U. S. BUREAU OF CENSUS, DEPT OF COMMERCE, 1954 CENSUS OF MINERAL INDUSTRIES 3, 14F-2, 14F-5.

<sup>28</sup> U. S. BUREAU OF MINES, *op. cit. supra* note 27, at 300.

Again, the Government (Br. 83) cites Census Bureau figures as showing that, in 1954, over 3,800,000 tons of "common clay and shale" were "shipped by miners" out of a total production of almost 30,000,000 tons. As explained above, note 27, these figures do not purport to show that 3,800,000 tons were sold, but only that this quantity was not processed at the same physical location as where the clay was extracted. Furthermore, the figures quoted are for the classification entitled "Clay, ceramic, and refractory minerals, not elsewhere classified," which is defined to include not

Certainly what is done by 10% of the producers of fire clay to 27% or less of the total production, or what is done by producers of shale to 4% of the total production does not establish what is normal or usual. *Generally and normally*, producers of fire clay and shale in the country must process their clay into burnt clay products in order to obtain their commercially marketable products. Thus, even if the determination of the "commercially marketable mineral product or products" is to be made on an industry-wide basis, the processes which such producers apply to obtain such burnt clay products are "the ordinary treatment processes normally applied" by producers of fire clay and of shale in order to obtain the "commercially marketable mineral product or products."

It follows, then, that, on the basis of the facts as to producers of fire clay and shale, such as this taxpayer, the Government can prevail only on the theory that "commercially marketable mineral product" is to be given the artificial meaning of a product "fit for commercial or industrial use," rather than its obvious meaning of a product which can in fact be sold on a commercial basis. It is, perhaps, for this reason that the Government has based its case here principally on this interpretation which, as we shall show below (pp. 106-09), it abandoned years ago after many courts had rejected it and which it did not present to the

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only "common clay and shale," but also "aplite, andalusite, dumortierite, kyanite, nepheline syenite, pinite, olivine, topaz, and zircon." U. S. BUREAU OF CENSUS, *op. cit. supra* note 27, at 3, 14F-2, 14F-10.

courts below or in its petition for certiorari to this Court.

### III

THE LEGISLATIVE HISTORY SUPPORTS THE TAXPAYER'S POSITION AND IS INCONSISTENT WITH THE GOVERNMENT'S THEORIES WHICH, IN FACT, CONGRESS HAS REPEATEDLY REJECTED.

The Government relies heavily on the legislative history of depletion, including cost and discovery value as well as percentage depletion, and the bulk of its brief (pp. 9-17, 35-80) is devoted to a lengthy discussion of such legislative history from 1913 to 1954.<sup>1</sup> Far from supporting the Government, the legislative history of percentage depletion supports the taxpayer's position and establishes the following principles:

(1) Congress has adopted the commercially marketable products rule to supply the base for computing the percentage depletion deduction. In so doing, it has recognized that various miners of

<sup>1</sup> In Appendix B to its Brief, the Government has gathered much legislative material dating from 1913 through 1954. In order to make available to the Court further material which we consider relevant, we are filing herewith the following: (1) Respondent's Appendix II which contains some additional material from the period of 1913 to 1954 and additional relevant material subsequent to 1954; and (2) copies of the Hearings held by the Ways and Means Committee in 1959 concerning the Treasury's legislative proposal to abolish completely the commercially marketable products rule. *Hearings Before the House Committee on Ways and Means on Mineral Treatment Processes for Percentage Depletion Purposes*, 86th Cong., 1st Sess. (1959) (hereinafter referred to as House Hearings, 1959).

the same ore or mineral may apply different processing to obtain their commercially marketable products and that, in some cases, they will have different commercially marketable products and, thus, different bases for depletion.

(2) In establishing the percentage depletion base, Congress has never drawn any distinction between processes generally termed "mining" and those generally termed "manufacturing" and has, in fact, repeatedly rejected the Treasury's attempts to draw such a distinction.

Before discussing the legislative history of percentage depletion, it is important to note that Congress has long allowed a depletion deduction unrelated to a taxpayer's actual cost or investment in his natural deposit. Discovery value depletion, first enacted by the Revenue Act of 1918, established as the basis for depletion the fair market value of the property after discovery of the mineral or ore deposit thereon.<sup>2</sup> Thus, Congress established a concept of depletion which departs from usual tax concepts in order to provide an incentive to discover, develop, and operate deposits of natural resources.<sup>3</sup>

When Congress turned from discovery value depletion to percentage depletion, it retained the principle

<sup>2</sup> Revenue Act of 1918, 40 STAT. 1057, § 214(a) (10) (Gov't App. B, pp. 3-4).

<sup>3</sup> Gov't Br. 37-38; House Hearings, 1925, p. 161 (Gov't App. B, p. 9); Partial Report of the Select Committee on Investigation of the Bureau of Internal Revenue, 1926, pp. 3, 19 (Gov't App. B, pp. 11, 12).



of allowing a tax-free recovery greater than actual cost in order to encourage the development of natural resources.<sup>4</sup> In fact, as has been pointed out to Congress, percentage depletion goes further than discovery value depletion in departing from a recovery of cost because it continues as long as the deposit is operated, whereas the deduction for discovery value depletion terminated when such value was recovered.<sup>5</sup>

The Treasury has long fought percentage depletion as being over generous and has long sought to have it reduced or eliminated.<sup>7</sup> At the same time, the Treas-

<sup>4</sup> House Debate, 1947, 93 Cong. Rec. 9628 (Gov't App. B, p. 237). House Hearings, 1959, pp. 22, 27, 53. In the 1959 Hearings, this fact was recognized by statements made by members of Congress, by the Treasury representative, and by a statement quoted from a report made in 1952 by the President's Materials Policy Commission.

<sup>5</sup> Joint Committee Report, 1930, p. 14 (Gov't App. B, p. 73).

<sup>6</sup> See *Commissioner v. Southwest Exploration Co.*, 350 U.S. 308, 312 (1956), where this Court, after stating that depletion is designed "to permit a recoupment of the owner's capital investment in the minerals," went on to state:

"The present allowance, however, bears little relationship to the capital investment, and the taxpayer is not limited to a recoupment of his original investment. The allowance continues so long as minerals are extracted, and even though no money was actually invested in the deposit."

<sup>7</sup> As early as 1934, the Treasury recommended the elimination of percentage depletion. (Gov't App. B, p. 138). It has tried continually since then to eliminate or reduce it and has opposed its extension to other minerals. One reason stated in the President's message vetoing the Revenue Act of 1943 was the provision thereof extending percentage depletion to certain minerals. 90 Cong. Rec. 1958, 1959 (1944) (Resp. App. II, p. 78). The Act was passed over the Presidential veto.

ury has fought the commercially marketable products rule for computing it. Congress, however, has refused to accede to the Treasury's wishes; it has continued and extended this type of depletion and has adhered to the commercially marketable products rule. It is for Congress to make the laws and the legislative history clearly shows that Congress favors percentage depletion.

**A. By enacting percentage depletion computed on the basis of the commercially marketable products rule, Congress intended to provide a simple and easily applied method of computing the depletion deduction.**

The percentage depletion deduction is computed as a percentage of a dollar base termed "gross income from the property" (but is limited to 50% of "net income of the taxpayer . . . from the property"). Its application to any given taxpayer is exceedingly simple, once this dollar base is determined. Congress has elected to determine the base by use of the commercially marketable products rule. This rule furnishes a simple method for computing the deduction, since the taxpayer can readily determine the commercially marketable products which he obtains and use their selling price (if he sells them at this point) or their established market value (if he processes them further) to compute his deduction.

Congress turned to percentage depletion because of the inequities and difficulties in the administration of discovery value depletion.\* In so doing, it was seeking

\* The Government in its brief (pp. 11, 12, 16, 40-41, 70 (Heading D), 71) repeatedly states that discovery value depletion was inequitable because it discriminated against small miners. It is true

a simple rule of easy application which would avoid the necessity of placing a "value" on a mine,<sup>9</sup> but not necessarily one that would provide the same dollar depletion deduction for all producers of the same ore or mineral. Before Congress extended percentage depletion to metal mines, the Staff of the Joint Committee

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that discovery value depletion was criticized because small miners did not have the funds required to contest the Treasury's determinations of the value of their mines. House Hearings, 1927-1928, pp. 506, 507, 508, 511 (Gov't App. B, pp. 38, 41, 45-46).

This, however, was merely one result of a basic fault of discovery value depletion, i.e., the difficulty of attempting to value a mine. Partial Report of the Select Committee on Investigation of the Bureau of Internal Revenue, 1926, pp. 3, 115-16 (Gov't App. B, pp. 11, 15); Senate Debate, 1926, 67 Cong. Rec. 3762 (Gov't App. B, p. 26); Joint Committee Report, 1930, pp. 1, 2 (Gov't App. B, pp. 67-68, 69); House Hearings, 1932, pp. 328, 331 (Gov't App. B, pp. 110, 112); House Hearings, 1951, pp. 1571-72, 1572-73 (Gov't App. B, pp. 291, 292).

Congress was told, in fact, that no two engineers could ever agree on a valuation, thus causing endless disputes. Senate Hearings, 1926, pp. 158, 177 (Gov't App. B, pp. 18, 19); House Debate, 1927-69 Cong. Rec. 599 (Gov't App. B, p. 48).

There were also other basic faults and inequities explained to Congress. For example, the discovery value of a given mine depended on the fortuitous circumstance of whether that mine was discovered in a time of prosperity or of depression. Joint Committee Report, 1930, p. 2 (Gov't App. B, p. 70).

<sup>9</sup> Partial Report of the Select Committee on Investigation of the Bureau of Internal Revenue, 1926, p. 116 (Gov't App. B, p. 15); Senate Hearings, 1926, pp. 158, 177, 197 (Gov't App. B, pp. 18, 19, 21); Joint Committee Report on Depletion, 1927, p. 13 (Gov't App. B, pp. 33-34); House Hearings, 1927-1928, pp. 161, 506, 508, 510 (Gov't App. B, pp. 36, 37-38, 40-41, 45); House Debate, 1927-69 Cong. Rec. 599 (Gov't App. B, p. 49); Joint Committee Hearings, 1930, pp. 6, 58 (Gov't App. B, pp. 90, 103); House Hearings, 1932, p. 341 (Gov't App. B, p. 117); Senate Hearings, 1932, p. 229 (Gov't App. B, p. 125).

on Internal Revenue Taxation prepared a report (the so-called Parker Report) which considered alternative methods of computing depletion: the "fixed rate per unit method," percentage depletion based on gross income, and percentage depletion based on net income. The first method would allow a fixed amount of depletion per pound for the metal sold and, thus, treat all miners of the same ore in exactly the same way. The Parker Report itself recommended against this method, one of the reasons being the very fact that it would treat all miners of an ore the same and not reflect the difference in the value of various grades of ores.<sup>10</sup> Congress has never given further consideration to this method. The Report also recommended against percentage depletion based on gross income because it appeared "to produce inequities in the case of certain industries."<sup>11</sup> This report recommended a deduction based on "net income from the property" after a reasonable amount of the net income has been allocated to the plant investment.<sup>12</sup> However, after extensive hearings,<sup>13</sup> at which arguments were presented for both gross income and net income methods, Congress chose the simple method based on gross income from the property.

<sup>10</sup> Joint Committee Report, 1930, pp. 12-13 (Resp. App. II, pp. 76-77).

<sup>11</sup> *Id.* at 3 (Gov't App. B, p. 71). See also Senate Hearings, 1926, p. 179 (Gov't App. B, p. 20).

<sup>12</sup> Joint Committee Report, 1930, pp. 14, 22 (Gov't App. B, pp. 73, 74).

<sup>13</sup> Joint Committee Hearings, 1930 (Gov't App. B, pp. 88-107); House Hearings, 1932 (Gov't App. B, pp. 108-30).

**B. Congress** has always intended the commercially marketable products rule and codified it in 1943 because the Treasury, which had originally accepted it, was attempting to modify it.

The statutory definition of "gross income from the property" involved in this case was enacted by the Revenue Act of 1943. It was, however, made retroactive to 1932 and the Senate Finance Committee Report stated that it "expresses the congressional intent of these provisions as first included in the law, and is in accord with the original regulations and the Bureau practices and procedures thereunder."<sup>14</sup> Consequently, to understand this legislative history, it is necessary to go back to the Revenue Act of 1932 and the original interpretation of the depletion provisions of that Act.

Congress in 1932 extended percentage depletion to coal, sulfur, and metal mines;<sup>15</sup> the statute, however, did not define "gross income from the property."

Guidance as to the meaning of the statute was supplied by the so-called Shepherd Report (Gov't App. B.

<sup>14</sup> S. REP. No. 627, 78th Cong., 1st Sess. 23-24 (1943) (Gov't App. B, p. 211).

<sup>15</sup> Revenue Act of 1932, 47 STAT. 169, § 114(b)(4) (Gov't App. B, p. 134). Previously, in 1926, percentage depletion had been granted to oil and gas: Revenue Act of 1926, 44 STAT. 9, § 204(c) (Gov't App. B, p. 31). These minerals are commercially marketable as they come from the ground and there are established, posted field prices for them at that point. Joint Committee Report on Depletion, 1927, p. 13, (Gov't App. B, p. 33); Joint Committee Hearings, 1930, pp. 50, 110 (Gov't App. B, pp. 101, 105); House Hearings, 1932, pp. 339, 341 (Gov't App. B, pp. 115, 116). Gross income from the property as to oil and gas is the market value of such crude products and the statutory definition of "gross income from the property" in Section 114 (b) (4) (B), the provision here involved, was not even made applicable to them.



pp. 76-87) which, in 1929, had proposed percentage depletion for metal mines based on "gross income from the property". The Government terms this the "definitive work on the subject," (Bf. 48) Shepherd reviewed the market situation as to various ores, and tentatively recommended a definition of "gross income from the property" for the regulations.<sup>16</sup> As to all ores, except those of gold, silver, and copper, Mr. Shepherd recommended that the market price of the crude ore or the "net smelter return" (the price miners receive from smelters for their concentrate) be used to compute "gross income from the property," since those ores are commercially marketable in the crude or concentrated form.<sup>17</sup> For gold, silver, and copper ores, Shepherd recommended that the product actually disposed of by the taxpayer be used, since in many cases the mine owners applied processes beyond the concentrate stage.<sup>18</sup>

<sup>16</sup> Joint Committee Report, 1930 (App. XXXI, Shepherd Report), p. 71 (Gov't App. B, p. 87).

<sup>17</sup> Thus, iron ore is marketable in crude form while non-ferrous metal ores which are to be smelted are marketable in concentrate form and are generally sold to smelters. Joint Committee Report, 1930 (App. XXXI, Shepherd Report), pp. 71, 69-70 (Gov't App. B, pp. 86, 83-84); see also Gov't Br. 29 p. 14, 8.

<sup>18</sup> It is also significant that Shepherd based his recommendation of a 15% rate for metal mines on figures showing that the average discovery value depletion was equivalent to about 17% of "gross sales" and that "gross sales" was computed as the price of the finished metals in the case of copper, lead, gold, and silver. Joint Committee Report, 1930 (App. XXXI, Shepherd Report), pp. 65-66 (Gov't App. B, pp. 80-81); Memoranda from the American Mining Congress to the Treasury, November 1932 (Resp. App. II, pp. 141-45); Silver Subcommittee Hearings, 1942, pp. 1008-09 (Gov't App. B, pp. 186-88).

After the Revenue Act of 1932, the Treasury issued regulations containing four lists of allowable processes applicable to coal, sulfur, and the various ores.<sup>19</sup> Subsequent controversy centered around the fourth list, applicable to "lead, zinc, copper, gold, or silver ores and ores which are not customarily sold in the form of the crude mineral product." The processes listed were:

"...crushing, concentration (by gravity or flotation), and other processes to the extent to which they do not beneficiate the product in greater degree (in relation to the crude mineral product on the one hand and the refined product on the other) than crushing and concentrating (by gravity or flotation)."

There are no published rulings showing how this regulation was interpreted, but other materials make it clear that the Treasury followed the commercially marketable products rule. When the regulation was drafted, representatives of the mining industry complained that it did not express the Congressional intent.<sup>20</sup> A statement later submitted to Congress by L. H. Parker, who had been Chief of the Staff of the Joint Committee on Internal Revenue Taxation and prepared the Parker Report (p. 81 & n.10 *supra*), and who participated in drafting the Revenue Act of 1932<sup>21</sup> explained:

<sup>19</sup> U. S. Treas. Reg. 77, Art. 221(g) (1933) (Gov't App. B, pp. 135-37).

<sup>20</sup> Memoranda from the American Mining Congress to the Treasury, November 1932 (Resp. App. II, pp. 132-60).

<sup>21</sup> House Hearings, 1932, pp. 336-37 (Gov't App. B, p. 112).

"The mine operators protested the definitions drafted by the Commissioner for inclusion in the regulations on the grounds that they did not express the clear intent of Congress. As a result, a group of mine operators and their representatives met with the officials of the Treasury late in December 1932 to discuss the matter. In this conference, *it was agreed the definitions drafted by the Commissioner did not express the intent of Congress.* However, as the regulations containing the definitions drafted by the Commissioner had, in the interim, been printed in bound form and been delivered to the Treasury Department and were ready for issuance, the Treasury representatives expressed reluctance to withdraw said regulations on the ground such a change could not be made and have the regulations issued in time for use in connection with the returns due to be filed March 15, 1933. To meet this situation, *it was proposed that the regulations be issued as printed with the understanding the definitions would be interpreted and applied according to the meaning of the act as agreed to in that conference.* The operators agreed to this procedure. The regulations were thus issued and the definitions were applied as agreed to up to about the latter part of 1938." (Italics ours.)<sup>22</sup>

Pursuant to this agreement, cyanidation and amalgamation of gold and silver ores, leaching of copper ores,

<sup>22</sup> House Hearings, 1947, p. 3283 (Resp. App. II, p. 82). See also Senate Hearings, 1943, p. 527 (Gov't App. B, p. 202).

and the furnacing of quicksilver ores were allowed,<sup>23</sup> although these processes go beyond concentration by gravity or flotation.<sup>24</sup> Smelting, however, was not allowed.<sup>25</sup> Thus, the Treasury did not go as far as Shepherd had recommended as to gold, silver, and copper ores, but did allow as to these ores certain processes which take them beyond the concentrate stage. Since cyanidation, leaching and furnacing quicksilver ores are all metallurgical processes involving chemical changes, just as smelting is, it is obvious that the standard used was that of the commercially marketable product.<sup>26</sup>

By allowing these various processes, however, the Treasury did not treat all miners of the same ore in the same way. For example, cyanidation of gold ore and the leaching of copper ore are alternatives to smelting for extracting the metal from the ore, and, thus, the depletion base for miners of these ores varied, depending on the processes used.<sup>27</sup>

<sup>23</sup> House Hearings, 1942, p. 1199 (Gov't App. B, p. 152); Silver Subcommittee Hearings, 1942, p. 1010 (Gov't App. B, p. 189); Senate Hearings, 1943, p. 527 (Gov't App. B, p. 203); Fernald, *Depletion and Related Problems Under the Revenue Act of 1942*, 21 TAXES 143 (Gov't App. B, p. 484).

<sup>24</sup> Silver Subcommittee Hearings, 1942, p. 736 (Gov't App. B, pp. 154-55).

<sup>25</sup> Senate Hearings, 1950, p. 782 (Gov't App. B, pp. 279-80); Fernald, *supra* note 23.

<sup>26</sup> See Resp. App. II, pp. 6-8.

<sup>27</sup> Resp. App. II, pp. 10-11. Furthermore, these regulations (Gov't App. B, p. 136) specifically allowed as to coal the processes of cleaning, breaking, and sizing (as well as loading for shipment); some types of coal are sold without the application of all of these processes. Also, sorting and concentrating were allowed as to iron ore, although these are not necessary to make all types of iron ore marketable. See Resp. App. II, pp. 8-9 and Gov't Br. 29 n.14.

Beginning about 1940, however, the Treasury changed its original position under the 1932 regulations and abandoned the commercially marketable products rule as to certain ores. Thus, it began to disallow processes such as cyanidation, leaching, and the furnacing of quicksilver ores.<sup>28</sup> This change in policy was fully explained to Congress in 1942.<sup>29</sup> The Treasury based its new position on the same ground as it urges here, *i.e.*, a theoretical distinction between mining and manufacturing. Thus, Congress was told that the Treasury was disallowing these metallurgical processes because they involved chemical changes and altered the character of the mineral.<sup>30</sup> This was explained on the theory that a miner who applied processes to his concentrates supplied his own market.<sup>31</sup>

"They come back and say, 'Well, if the company itself owns a cyanide plant and refinery we have got there a *theoretical computation that they are selling the concentrates to themselves* after they

<sup>28</sup> House Hearings, 1942, pp. 1199, 1202 (Gov't App. B, pp. 152-53); Silver Subcommittee Hearings, 1942, pp. 762, 858, 859 (Gov't App. B, pp. 161-62, 172-73, 174); House Hearings, 1947, p. 3283 (Resp. App. II, pp. 82-83); Fernald, *supra* note 23, p. 86.

<sup>29</sup> A member of Congress was "astonished" to learn that the Treasury was seeking to cut off the computation of the deduction for cinnabar ore before income could be realized from the ore. House Hearings, 1942, p. 1202 (Gov't App. B, pp. 152-53). The change in policy, however, was not expressed in any published regulation or ruling. Senate Hearings, 1943, pp. 527-28 (Gov't App. B, p. 203).

<sup>30</sup> Silver Subcommittee Hearings, 1942, pp. 858, 859, 860, 861 (Gov't App. B, pp. 172, 174, 176, 177, 178).

<sup>31</sup> Silver Subcommittee Hearings, 1942, p. 762 (Gov't App. B, p. 161).



get them through the flotation, and subtracting the cost of the cyaniding." (Italics ours.)<sup>32</sup>

The Treasury then, as now, justified its position on the basis that all taxpayers should be treated alike and feared that otherwise depletion for iron ore would be based "on the value of the steel rolled into finished shapes."<sup>33</sup>

Congress took no action in 1942; the Treasury opposed corrective legislation and represented that it would handle the question administratively by returning to its original practices under the regulations.<sup>34</sup> However, the Treasury did not do so,<sup>35</sup> and, in 1943, representatives of the metal ore producers again came to Congress with the same complaint.<sup>36</sup> This time Congress did act in the Revenue Act of 1943 by adding Section 114(b)(4)(B) to the Code, defining "gross income from the property" and specifically writing the commercially marketable products rule into the

<sup>32</sup> Compare the Government's statement here (Br. 18-19):

"If all miners of a particular mineral become integrated, thus providing their own market for the mineral product, the depletion base does not thereby come to comprehend the processes of fabrication and to multiply many times over."

See also Gov't Br. 84-85.

<sup>33</sup> Silver Subcommittee Hearings, 1942, pp. 763-64, 860. (Gov't App. B, pp. 164-65, 176).

<sup>34</sup> Senate Debate, 1942, 88 CONG. REC. 8033 (Gov't App. B, pp. 196-98).

<sup>35</sup> *Secretary's Report, American Mining Congress Reviews Its Activities in 1942*, 29.2 MINING CONGRESS JOURNAL, March 1943 issue, p. 22 (Gov't App. B, pp. 471-72).

<sup>36</sup> Senate Hearings, 1943, pp. 527-29, 928 (Gov't App. B, pp. 201-07, 209).

statute.<sup>37</sup> Also, to end controversy, Congress specifically listed as ordinary treatment processes the metallurgical processes which the Treasury had originally allowed in 1932 but which it later tried to exclude. The Senate Finance Committee, which added the section to the revenue bill, explained it as follows:

"The purpose of the provision is to make certain that the *ordinary treatment processes which a mine operator would normally apply to obtain a marketable product* should be considered as a part of the mining operation, and to give reasonable specification of what are to be considered such processes for various kinds or classes of mines.

"The law has never contained such a definition, and its absence has given rise to numerous disputes. The definition here prescribed expresses the congressional intent of these provisions as first included in the law, and is in accord with the original regulations and the Bureau practices and procedures thereunder. It is therefore made retroactive to the date of such original provisions."

(Italics ours.)<sup>38</sup>

The Government in its brief states (p. 14) that, in 1943, Congress "wrote the 1932 Treasury Regulations

<sup>37</sup> Revenue Act of 1943, 58 STAT. 21, § 124 (Gov't App. B, pp. 224-25). As explained above, p. 78 n.7, this Act was passed over the President's veto.

<sup>38</sup> S. REP. NO. 627, 78th Cong., 1st Sess. 23-24 (Gov't App. B, pp. 210-11).

into the statute" and then characterizes Section 114-(b)(4)(B) variously as a "codification" of the Treasury's 1932 regulations (Br. 55, 74 n.60), of the "essential features" of these regulations (Br. 73), of the Treasury's "original regulations and practices" (Br. 63), of the "original administrative practice" (Br. 58, Heading 4), and of "concepts which had developed over the preceding thirty years." (Br. 36) As a matter of fact, the language which is crucial to this case, that mining shall include "the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products," has no counterpart in any prior statute, regulation, or ruling.

It is perfectly clear that the statute is not a codification of the 1932 regulations.<sup>39</sup> The entire portion of the statute preceding the four lists of processes is completely different from the regulations. The regulation requires *excluding* the cost of all processes, except those *specifically* named, which are applied to obtain the "*first marketable product.*" The statute, however, states that "mining" shall *include* "the ordinary treatment processes normally applied by mine owners or operators in order to obtain the *commercially marketable mineral product or products.*" Furthermore, the lists of processes are broader in the statute. As a matter of fact, the only points of similarity between the regulation and the statute are that both start with a

<sup>39</sup> U. S. Treas. Reg. 77, Art. 221(g) (1933) (Gov't App. B. pp. 135-37).

statement that "gross income from the property" shall "mean," and both have four lists of processes.<sup>40</sup>

Furthermore, the Finance Committee Report states that Section 114(b)(4)(B) "expresses the congressional intent of these provisions as first included in the law." The Treasury itself recognized in 1932 that its regulations did not follow that intent, and, in fact, it did not originally plan to apply them as written (p. 85 *supra*). Actually, all the Finance Committee Report states is that the statute "is *in accord* with the original regulations and *the Bureau practices and procedures* thereunder." As shown above, the Treasury originally applied the commercially marketable products rule under these regulations, although it was not stated in them, and Congress obviously meant that it was adopting this rule which had originally been applied by the Treasury in interpreting and applying the regulations.

**C. Congress has continued to extend percentage depletion to additional minerals, always adhering to the commercially marketable products rule and rejecting the Treasury's attempts to modify or abolish it.**

Beginning in 1942, Congress granted percentage depletion to additional minerals until, finally, in 1954, it granted it to all minerals.<sup>41</sup> In so doing, Congress obviously intended to provide an incentive to discover

<sup>40</sup> See also the discussion of the Government's argument in *Dragon Cement Co. v. United States*, 244 F.2d 513, 519 (1st Cir. 1957), cert. denied, 355 U.S. 833 (1957) (Resp. App. II, pp. 11, 26).

<sup>41</sup> The only exceptions are soil; sod; dirt; turf; water; mosses; and minerals from sea water, the air, or similar inexhaustible sources. INT. REV. CODE OF 1954, § 613(b)(6) (Resp. App. II, pp. 112-13).

and develop deposits of the various minerals, and it recognized that it was not merely providing a return of the mine owner's capital.<sup>42</sup> It is also obvious that Congress has adhered to the commercially marketable products rule for determining the depletion base, amending the statute in 1950 when the Treasury tried to modify that rule, and refusing to change it when the Treasury attacked it in 1954, 1958, and 1959.

1. *In 1950, Congress specifically included "transportation" in "mining" because the Treasury was seeking to exclude it and thereby modify the commercially marketable products rule.*

In 1950, Congress amended Section 114(b)(4)(B) to add to "mining" transportation of the ores and minerals from the point of extraction to the mill or plant where the ordinary treatment processes are applied.<sup>43</sup> Obviously, transportation is not within any commonly understood definition of "mining." However, where there is such transportation, it must be included in the depletion base to follow the statutory scheme of using the selling price of the commercially marketable products as the depletion base. The Treasury had originally allowed "gross income from the

<sup>42</sup> The Government states (Br. 70) that, "The industry has repeatedly urged [percentage depletion] as a fair and equitable method of measuring the exhaustion of capital assets." Actually, producers of the various minerals, as well as others, have urged percentage depletion as a method of tax relief which provides both the incentive and funds to prospect for and develop new deposits of the various ores and minerals. See, for example, the excerpts from the House Hearings, 1947, 1950, and 1951, reproduced in Resp. App. II, pp. 79-80, 83-106.

<sup>43</sup> Revenue Act of 1950, 64 STAT. 906, § 207 (Gov't App. B, p. 287).



property" to be computed without adjustment for such transportation, but had recently changed its position.<sup>44</sup> Thus, again, as in the Revenue Act of 1943, Congress had to act to prevent the Treasury's whittling away at the commercially marketable products rule.

**2. In 1951, when Congress granted percentage depletion to fire clay and shale, it intended that the deduction be computed in accord with the commercially marketable products rule.**

In 1951, when Congress added fire clay and shale to the minerals granted percentage depletion, there is nothing in the legislative history to show that Congress intended that the allowance for these minerals should be computed in any way other than that by which it is computed for all other minerals, i.e., under the commercially marketable products rule.<sup>45</sup> A letter written on June 4, 1955, by Senator George, Chairman of the Senate Finance Committee in 1951, to T. Coleman. An-

<sup>44</sup> Senate Hearings, 1950, pp. 771, 772 (Gov't App. B, pp. 275, 276).

<sup>45</sup> In an attempt to show that the "commercially marketable mineral product" of fire clay is raw clay, the Government discusses the testimony in 1950 of a representative of the refractories industry, who requested percentage depletion on "the 'value' of 'raw materials used.'" (Gov't Br. 79-80). Actually, this witness did not request depletion for "fire clay" as such at all. Instead, he sought depletion for "refractory clays and quartzite," and stated that this term would not include "deposits of clays and silica rock not used for refractories." He argued against using the term "fire clay" because it also embraces other clays "not distinctively refractory minerals." House Hearings, 1950, pp. 449-50 (Gov't App. B, pp. 337-38). Taxpayer is not in the refractory industry and does not produce refractory products. Obviously, when, in 1951, the subsequent Congress allowed percentage depletion for "refractory and fire clay," it had in mind clays different from those mentioned by this witness.

draws, then Commissioner of Internal Revenue, explains with specific reference to brick and tile clay (which was also granted percentage depletion in that year) that the commercially marketable products rule was specifically intended:<sup>46</sup>

"... [T]he statute defining mining for purposes of computing depletion allowance for federal income and excess profits tax purposes does not exclude manufacturing processes so long as they are ordinary processes normally and necessarily used in obtaining commercially marketable mineral products.

"I personally recall the discussion in executive session between members of the Senate Finance Committee when this statute was under consideration. At the time it was not only understood but I pointed out what I knew and believed to be the facts about brick manufacture. . . . Brick clay at this time has no commercial value until it is baked or cooked. The Senate Finance Committee certainly understood this clearly, before the Act, giving depletion allowance to brick clay, was passed."<sup>47</sup>

<sup>46</sup> This letter is referred to and quoted in part in the House Hearings, 1959, pp. 258, 264, and was reproduced in full with Senator George's approval, in *Brick and Clay Record*, Vol. 130, No. 1, at 87-88 (January 1957). It is set forth in full in Resp. App. II, pp. 163-65.

<sup>47</sup> See also House Debate, 1950, 96 CONG. REC. 15590 (Gov't App. B, pp. 286-87) on the Revenue Act of 1950, which, as explained above, specifically added certain transportation to "mining." The

Apparently to try to show the contrary, the Government states (Br. 65-66) that the Senate passed an amendment to the Technical Changes Act of 1949 which would have extended percentage depletion to "all other nonmetallic clays and minerals" and concludes that "it is significant that a broad extension of the allowance to numerous additional minerals was not thought to require any modification of the method of computing the allowance"; it then quotes a statement in the Finance Committee Report that "It is not proposed to allow percentage depletion with respect to the value added as the result of grinding or other special preparation," because "many" of the extractors "sell these minerals in crude form."

The Government's argument could be interpreted as implying that the statement in the Finance Committee Report refers to "all other nonmetallic clays and minerals." Actually, this statement was made with reference only to perlite and diatomaceous earth, the only minerals granted percentage depletion by the bill as reported by the Finance Committee and to which this Committee Report relates.<sup>48</sup> The amendment extending depletion to "all other nonmetallic clays and minerals" was added *subsequently* on the floor of the Senate.<sup>49</sup> The entire amendment, as to all minerals

statements of Representative Jenkins, a member of the Ways and Means Committee, show that he contemplated that, if percentage depletion were extended to clay, the processes of making brick, would be included in "mining."

<sup>48</sup> S. REP. No. 831, 81st Cong., 1st Sess., 9-10 (Gov't App. B, pp. 246-47).

<sup>49</sup> Senate Debate, 1949, 95 Cong. REC. 12994.

Including perlite and diatomaceous earth, was removed by the Conference Committee, "with the understanding that the entire matter of percentage depletion will be considered early next year after full study and hearings."<sup>50</sup> It is significant that the subsequent Congress which did enact percentage depletion for these minerals (in 1951) after further study made no such statement.

**3. In 1954, Congress reaffirmed the commercially marketable products rule and rejected an attempt to abolish it as to brick and tile clay.**

In the hearings on the Internal Revenue Code of 1954, Congress was requested by industry representatives to add, and did add, to the ordinary treatment processes specifically listed in the statute, the pulverization of talc; the burning of magnesite; the sintering and nodulizing of phosphate rock; and dust allaying and treating to prevent freezing of coal.<sup>51</sup>

<sup>50</sup> H. R. REP. NO. 1412, 81st Cong., 1st Sess. II (Gov't App. B, p. 248).

<sup>51</sup> INT. REV. CODE OF 1954, § 613(c) (4) (A), (E) (Resp. App. II, p. 114). House Hearings, 1953, pp. 2035-42, 2059-60 (Gov't App. B, pp. 448-51, 394-95); Senate Hearings, 1954, pp. 1334-37, 1409-13 (Gov't App. B, pp. 398-401, 342-48).

Although these processes must be applied to talc and magnesite to obtain commercially marketable products, the Treasury had sought to exclude them. *Townsend v. The Hitchcock Corp.*, 232 F. 2d 444 (4th Cir. 1956) and *International Talc Co.*, 15 T.C. 981 (1950), as to talc, and *Northwest Magnesite Co. v. United States*, 58-1 U.S.T.C. ¶ 9394 (E.D. Wash. 1958), as to magnesite.

Treatment to prevent freezing is applied to coal only where and when the climate requires it; dust allaying is applied to only about 9% of the coal produced, but is necessary to obtain a particular commercially marketable product of coal (i.e., coal for domestic use). See Senate Hearings, 1954, pp. 1409-13 (Gov't App. B, pp. 343-48; Resp. App. II, p. 9).

The Treasury, on the other hand, sought to abolish the commercially marketable products rule as to brick and tile clay and substitute its theory distinguishing between mining and manufacturing. The Ways and Means Committee announced on February 18, 1954, during its consideration of the Internal Revenue Code of 1954, that such a provision was being added to the draft of the bill and stated that the law "has been interpreted [by T.D. 6031, approved July 14, 1953, discussed below, p. 106] in the same way as specifically provided by the Committee's bill."<sup>52</sup> A few days later, on February 24, 1954, the Committee reversed its action and stated:

"The Committee reconsidered a previous decision it made with respect to percentage depletion on brick and tile clay. Previously the Committee had agreed to include a specific provision in the bill that ordinary treatment processes with respect to brick and tile clay were not to include 'molding, shaping, extruding, firing, or burning,' in order to resolve a question which exists under present law. The Committee agreed not to include this specific phrase, thus leaving the treatment of these processes to be determined under existing law."<sup>53</sup>

<sup>52</sup> Committee on Ways and Means, House of Representatives, Press Release #24, Feb. 18, 1954 (Resp. App. II, pp. 107-08).

<sup>53</sup> Committee on Ways and Means, House of Representatives, Press Release #27, Feb. 24, 1954 (Resp. App. II, p. 108).

The District Court decided *Cherokee Brick & Tile Corp. v. United States*, 122 F. Supp. 59 (M.D. Ga. 1954), *aff'd*, 218 F.2d 424 (5th Cir. 1955), involving brick and tile clay, in favor of the taxpayer on June 4, 1954, and the Internal Revenue Code of 1954 did not pass the Senate until July 2, 1954. Yet Congress did not act in 1954 to change the result in that case and, in fact, has not since acted.



**4. In 1958, Congress refused to adopt the Treasury's proposal to abolish the commercially marketable products rule as to clay and as to minerals used for cement.**

After Congress refused to act as to brick and tile clay in 1954, the Treasury made no further legislative attempts to change the commercially marketable products rule until, after long litigation and denial of certiorari by this Court, it accepted the unanimous holdings of the cases as to brick and tile clay and cement rock in T.I.R. 62, issued on October 18, 1957.<sup>54</sup> Promptly thereafter, however, on January 16, 1958, The Secretary of the Treasury asked Congress to enact the theories advanced here by the Government. He said:

"Last October, the Supreme Court denied a petition for certiorari in a series of cases dealing with the so-called cutoff point for percentage depletion in the manufacture of bricks and cement.

"*The net result of the cases is to apply the percentage depletion allowance to the price of finished manufactured products, bricks and cement, rather than to the value of the clay and the cement rock before it is manufactured.*

\* \* \* \* \*

"*The problem appears to arise from the application of the phrase 'the commercially marketable mineral product or products' in the statute. I recommend the law be revised to prevent these excessive depletion deductions. The revenue loss in*

<sup>54</sup> 1957 INT. REV. BULL. No. 43, at 51; 5 CCH 1957 STAND. FED. TAX REP. ¶ 6824; 4 P-H 1957 FED. TAX SERV. ¶ 76,726 (Resp. App. II, pp. 165-66).

the two industries directly covered by the cases is about \$50 million a year." (Italics ours.)<sup>55</sup>

On April 24, 1958, the Treasury submitted to Congress proposed legislation which would enact its position as to clay and as to minerals used for cement. The transmittal letter, from Dan Throop Smith, then Deputy to the Secretary of the Treasury, shows that the Treasury considered it settled that "manufacturing" processes could be "mining" under the statute and that it lacked confidence in the other arguments which the Government presents here:

*"... The result of the court decisions is that a taxpayer who extracts the mineral from the ground and applies processes thereto may base his depletion allowance on income from the commercially marketable product, regardless of whether or not his processes are manufacturing processes. It is believed that depletion on this scale is excessive and was not intended.*

*"In the absence of further legislation providing a specific cut-off point for other minerals and ores, this Department will continue to face substantial problems in determining for many mineral industries the stage at which taxpayers first obtain a commercially marketable mineral product. There is, for example, a question as to whether the stage*

<sup>55</sup> House Hearings, 1958, pp. 1097-98 (Resp. App. II, p. 115).

should be determined by reference to the taxpayer's own local market or the national market. In some cases the local market approach would have the effect of obtaining a different cut-off for the same mineral in different areas of the United States. *On the other hand, the national market approach, while establishing a uniform first commercially marketable product for an entire industry, would be difficult to apply in instances where there is no readily available data with respect to the minerals concerned. Moreover, there is a question as to whether the courts would accept the national market approach as the correct construction of the statute.*" (Italics ours.)<sup>56</sup>

Congress, however, took no action on this proposal; no hearings were held and no bill was introduced.

**5. In 1959, Congress refused to adopt the Treasury's proposal to abolish the commercially marketable products rule as to all minerals.**

The Treasury renewed its efforts to obtain legislation in 1959, recommending that the commercially marketable products rule be abolished for all minerals and ores. The President's Budget Message contained a statement as to the need for legislation in this area.<sup>57</sup> On January 26, 1959, the Secretary of the Treasury wrote to the Speaker of the House, stating:

<sup>56</sup> Treasury Proposal, 1958 (Resp. App. II, pp. 116, 118-19, 120).

<sup>57</sup> Presidential Budget for 1960—Message from the President of the United States (H. R. Doc. No. 15), 1105 CONG. REC. 816, 817-18 (1959) (Resp. App. II, pp. 123-24).

"It is now apparent under the court decisions that manufacturers of many other products may obtain depletion allowances based on gross income derived from the sale of finished products. . . .

"The problem arises because the term 'mining' is defined in the statute to include the ordinary treatment processes normally applied to obtain the 'commercially marketable mineral product or products' *which, in many instances, may be an expensive finished product.* Accordingly, in order to prevent excessive depletion allowances, *I recommend the immediate elimination of the phrase 'commercially marketable mineral product or products' from the statute and the substitution of a new definition of 'mining' which will specify the allowable treatment processes for the various minerals.*

"The proposed legislation would not only prevent a substantial loss in revenue, but would also help resolve difficult and complex problems in determining for many mineral industries the stage at which taxpayers first obtain a commercially marketable mineral product." (Italics ours.)<sup>58</sup>

On February 11, 1959, the Secretary submitted a legislative proposal to accomplish this purpose.<sup>59</sup> The Ways and Means Committee held five days of hearings on this proposal.<sup>60</sup> At these hearings, the Treasury

<sup>58</sup> Treasury Proposal, 1959 (Resp. App. II, pp. 124, 126).

<sup>59</sup> Treasury Proposal, 1959 (Resp. App. II, pp. 128-32).

<sup>60</sup> House Hearings, 1959. For the Court's convenience, copies of these Hearings are being filed herewith.

stated that "this legislative recommendation is one of the most important pieces of tax legislation which will be considered by the Congress this year" (House Hearings, 1959, p. 2), and presented to the Committee the same theories which it presents here. <sup>60</sup> It urged that only "mining" processes should be allowed and "manufacturing" processes should be disallowed (*Id.* at 7-9, 20, 50); <sup>61</sup> it argued that the present statute, as interpreted by the courts, creates discrimination among taxpayers, *accepting* the fact that the cases establish that different taxpayers may have different commercially marketable products (*Id.* at 18, 25, 35, 36, 43, 44, 47, 55); it argued that this interpretation will encourage "integration" (*Id.* at 4, 6, 29); and it submitted tables as to revenue loss identical to those it presented in its petition for certiorari in this case. The Treasury's proposal and arguments were received with a general lack of enthusiasm by the Ways and Means Committee. <sup>62</sup> Members of the Committee feared

<sup>60</sup> Inconsistently, however, the Treasury proposed to continue to allow certain processes (i.e., cyanidation, crystallization, precipitation, and leaching) which it recognized as "manufacturing" processes. House Hearings, 1959, p. 7. In addition, it developed a new but undefined concept of "neutral" processes, i.e., neither mining nor manufacturing, which apparently would be disallowed but which would not have the effect of making subsequent "mining" processes unallowable. *Id.* at 8-9.

<sup>62</sup> House Hearings, 1959, pp. 11-13; Pet. for Cert. 39-41 (App. C).

<sup>63</sup> For example, after hearing representatives of the brick and tile industry, Representative Mason stated (House Hearings, 1959, p. 270):

"In my opinion you three men, plus the testimony of Mr. Vinson, have placed the last nail in the coffin of that proposed scientific formula that the Treasury wants us to adopt as a basis for depletion allowance, instead of the commercially



that departure from the established commercially marketable products rule would create confusion<sup>61</sup> and put too much power in the hands of the Treasury to determine how to compute the depletion deduction.<sup>62</sup>

marketable value, which is a definite thing and can be arrived at definitely.

"So far as I am concerned that proposal is dead."

<sup>61</sup> For example, Representative Ikard stated (*Id.* at 45):

"It still looks to me as if, rather than bringing about uniformity of treatment, conceivably you could be developing more confusion and certainly an area in which there no doubt would be a great deal of litigation over this cutoff point."

Representative Simpson stated (*Id.* at 55):

"Certainly we have comparative stability. The Department has been told by the courts just where depletion is to apply, the amount of money, based upon decisions at hand, is not too large, in my judgment.

"Certainly it is a small price to pay for stability in a field where cases have been hanging open for years, 6, 7, or 8 years, because we have not been able to reach an administrative decision. I think we might advisedly retain something that gives us an element of certainty rather than adopt the terrific uncertainty that we would find from the approval of a new approach to this question."

<sup>62</sup> Thus, Representative Simpson stated (*Id.* at 54, 55):

"... But how do you think the country would profit from the uncertainties that are always incident and arise when individuals are given what can amount to the question of life or death over an industry? I am advised in some of the fields, certainly with respect to some corporations, the amount returnable or retainable by the taxpayer as a result of depletion allowance does represent economic life or death to the company.

"I wish you would come in with firm standards and tell us exactly what you want done in these different areas. I could listen and give it some consideration. But I personally cannot view with favor any proposal that further increases the position of power of individuals to hold life or death authority over any of our industries."

The Treasury's inability (discussed at pp. 109-12 *infra*) to develop a definite rule under its theories presented here, which are the same it presented to Congress, shows that these fears were not unjustified.

The Ways and Means Committee has not reported a bill and Congress has taken no further action.

**D. In summary, the legislative history supports taxpayer's position.**

- 1. Congress has consistently used the commercially marketable products rule to supply the base for computing the percentage depletion deduction. In so doing, it has recognized that various miners of the same ore or mineral may apply different processes to obtain their commercially marketable products and that, in some cases, they will have different bases for depletion.**

The legislative history makes it clear that Congress has always regarded the commercially marketable products rule as central to its concept of percentage depletion. Congress first enacted this rule specifically in 1943 because the Treasury, having first applied it, was departing from it.

Congress has recognized, in the listed processes, that various miners of the same ore or mineral will apply different processes to obtain their commercially marketable products and that, in some cases, they will have different commercially marketable products, and thus different bases for depletion.<sup>66</sup> Congress has never shown an intent to give all miners of the same mineral the same depletion deduction and, in turning to percentage depletion, actually rejected a method of fixed

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<sup>66</sup> See Resp. App. II, pp. 8-11.

rate per unit") that would have done exactly that. Congress has shown, instead, a consistent determination to maintain the commercially marketable products rule as a simple and practical means of determining the percentage depletion deduction.

**2. In establishing the percentage depletion base, Congress has never drawn any distinction between processes generally termed "mining" and those generally termed "manufacturing" and has in fact repeatedly rejected the Treasury's attempts to draw such a distinction.**

Congress has, in some cases, specifically included "manufacturing" processes (as the Government defines this term) in mining. Congress, in fact, enacted Section 114(b) (4)(B) because the Treasury was attempting to apply its "manufacturing" concept administratively at a time when the statute was not specific. In 1950, Congress specifically included in "mining" certain transportation, an item no one would ever consider to be "mining" within the commonly understood meaning, when the Treasury sought to whittle away at the commercially marketable products rule by excluding such transportation from the depletion base. And Congress in the last six years has rejected three direct attacks by the Treasury on this rule—as to brick and tile clay in 1954; as to clay and as to minerals used for cement in 1958; and as to all minerals and ores in 1959.

## IV

THE GOVERNMENT'S POSITION DOES NOT LEAD TO A CONSISTENT OR COHERENT MEANS OF CONSTRUING AND APPLYING THE STATUTE.

**A. The Government has developed many theories, none of which can be reconciled with the words actually used in the statute.**

The Government's argument that income from "manufacturing" processes cannot be included in computing the depletion base is not new. As we have shown (pp. 82-91 *supra*), Congress enacted Section 114(b)-(4)(B) in the Revenue Act of 1943, because the Treasury was then taking this same position. The Treasury returned to this position by amending its regulations in 1953,<sup>1</sup> after fire clay, shale, brick and tile clay, and other minerals had been granted percentage depletion in 1951. This amendment to the regulations was promptly challenged in court,<sup>2</sup> and the Government was then forced to try to square its position with the statutory language.

At first, it argued that "commercially marketable" means ready for use in "manufacture," the same position it takes here.<sup>3</sup> After losing two cases in the Courts

<sup>1</sup> T.D. 6031, 1953-2 CUM. BULL. 120, amending Section 29.23 (m)-1(f) of Treasury Regulations 111 (Resp. App. I, pp. 125-28 *infra*).

<sup>2</sup> *Cherokee Brick & Tile Co. v. United States*, 122 F. Supp. 59 (M.D. Ga. 1954), filed on September 3, 1953. The decision for the taxpayer was affirmed. 218 F.2d 424 (5th Cir. 1955).

<sup>3</sup> Thus the Government argued in the *Cherokee* case:

"The clay on which depletion is allowed has reached as fine and marketable a form as it ever will prior to becoming brick

of Appeals,<sup>4</sup> it turned its attention to "mineral product" and argued that a "manufactured" product cannot be a "mineral" product. After three Courts of Appeals rejected this argument,<sup>5</sup> it argued to this Court in a petition for certiorari in 1957 that "the depletion base ('gross income from mining') contemplated by Congress has reference to income received from a mineral product resulting from a definite pattern of treatment processes," which excludes "manufacturing."

After this Court denied the writ in 1957,<sup>7</sup> the Government dropped its "manufacturing" argument and the Revenue Service announced its acquiescence in the decisions holding that "manufacturing" processes are

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at the time it enters the pugmill. As clay, it is then in the form of a commercially marketable product. That the prohibitive expense involved in its transportation discourages an active market for the material cannot change the fact that it is ready for use in brick and tile manufacture." Brief for Appellant, p. 19, *United States v. Cherokee Brick & Tile Co.*, 218 F.2d 424 (5th Cir. 1955).

Compare the Government's use here (Br. 18, 21, 25, 26, 76, 78, 80, 85, 90) of "fit for commercial or industrial use."

<sup>4</sup> *United States v. Cherokee Brick & Tile Co.*, note 2 *supra*; *Townsend v. The Hitchcock Corp.*, 232 F.2d 444 (4th Cir. 1956).

<sup>5</sup> *Dragon Cement Co. v. United States*, 244 F.2d 513 (1st Cir. 1957), *cert. denied*, 355 U.S. 833 (1957) (Resp. App. II, p. 11); *United States v. Sapulpa Brick and Tile Corp.*, 239 F.2d 694 (10th Cir. 1956); *United States v. Merry Bros. Brick and Tile Co.*, 242 F.2d 708 (5th Cir. 1957), *cert. denied*, 355 U.S. 824 (1957).

<sup>6</sup> *Petition for Certiorari*, p. 13; *United States v. Merry Bros. Brick and Tile Co.*, No. 220, October Term, 1957.

<sup>7</sup> 355 U.S. 824 (1957). The Government also filed a petition for certiorari in *Dragon Cement Co. v. United States*, 244 F.2d 513 (1st Cir. 1957), which was also denied at the same time, 355 U.S. 833 (1957).



within the statutory definition of "mining" when applied to obtain the commercially marketable products.<sup>8</sup> Before the District Court in this case, the Government merely tried to show a market for taxpayer's fire clay and shale in crude form (pp. 28-40 *supra*). After being unsuccessful in this attempt, it shifted to a new position in the Court of Appeals, emphasizing the words "normally applied by mine owners or operators" and arguing that, for each "mining" industry, there is only one "commercially marketable" product which is the "cheapest" or "least processed" product which can be sold anywhere in the United States in more than negligible quantities.<sup>9</sup> The court below, as well as a number of other lower courts, rejected this argument.<sup>10</sup> The Government made the same argument in its petition for certiorari to this Court (Pet. for Cert. 14-17), stating that the issue here is "discrete," "entirely distinct," and "distinct" from the issue in earlier cases

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<sup>8</sup> T.I.R. No. 62, 1957 INT. REV. BULL. No. 43, at 51 (Resp. App. II, pp. 165-66).

<sup>9</sup> The Court of Appeals stated (R. 269-70) that the argument that depletion could not be computed on the basis of the selling price of "manufactured" products "has definitely been laid to rest." The Government stated in its brief in the Court of Appeals (p. 14):

"It is our position that the definition of 'mining' in Section 114(b)(4), as implemented by the definitions of 'ordinary treatment processes,' contemplates a single product as the depletable product for each mineral, albeit in some instances—namely, where the mineral is not marketable in mineral form—that product will necessarily be a manufactured product."

<sup>10</sup> *E.g.*, Commissioner v. Iowa Limestone Co., 269 F.2d 398 (8th Cir. 1959) (Resp. App. II, p. 28); Albin C. Halquist, 33 T.C. 304 (1959) (Resp. App. II, p. 44).

where it tried to exclude all "manufacturing" from "ordinary treatment processes." (Pet. for Cert. 5 n.5, 12, 14) <sup>11</sup> Now that certiorari has been granted, it interprets "commercially marketable" as "fit for commercial or industrial use" or ready for manufacture, returning to the original argument which it first made years ago but which it had not previously made in this case.

None of these theories advanced by the Government can be reconciled with the words used by Congress in adopting the commercially marketable products rule. The Government's difficulty and vacillation in attempting to square its basic position (distinguishing "mining" from "manufacturing") with the statute shows that it is trying to read into the statute something which is not there.

**B. The Government has not taken a position as to how this taxpayer's depletion deduction should be computed under its interpretation.**

Although the Government asserts (Br. 17) that "The application of the statute (as we interpret it) to this case presents no difficulty," it nowhere states how the statute should be applied to this taxpayer; instead, it asks (Br. 91) this Court to reverse and remand so that taxpayer's "gross income from mining" may be determined in the light of the correct legal criteria"—which the Government expects this Court to develop.

<sup>11</sup> In its petition for certiorari, the Government stated (p. 17):

"What is involved here is not the question whether manufacturing processes are includable in the depletion base in situations where it is necessary to do some manufacturing to get the first commercially marketable product."

The failure of the Government to take a position as to how the taxpayer's depletion deduction should be computed shows the weakness of its case.

The Government says only (Br. 80, Heading III) that taxpayer's depletion deduction must be computed "with reference to" the crude minerals (raw fire clay and shale).<sup>12</sup> If a "market or field price" is to be used,<sup>13</sup> what is the relevant area which must be studied to determine it? Should it be determined on a "national" basis or a "local" basis? If a "local" basis is used, what is the critical local market area? Is it that area in which the taxpayer could be competitive in a practical, business sense? There is no such area in the case of this taxpayer. If some other area is to be used, there is no logical basis for using any area short of the whole

<sup>12</sup> In the Court of Appeals, the Government even showed doubt as to whether raw clay is the first commercially marketable product under its theory in that court, and stated in its brief (p. 28):

"If the Court accepts our legal position—that is, that the depletable product is that commercially marketable product which is obtainable from the particular mineral with the least processing—but is not sufficiently convinced that raw fire clay and shale are the first commercially marketable products of fire clay and shale deposits, we suggest that the case be remanded for further evidence as to the first marketable product. . . ."

It went on to suggest in its brief (p. 29 n.18) that "the next commercially marketable product after raw clay may be ground fire clay" and that "the next possible commercially marketable product obtainable with the least processing may be common brick," since "except under unusual circumstances, brick is marketable in most any area."

<sup>13</sup> Cf. U. S. Treas. Reg. 111, § 29.23(m)-1(f) (Resp. App. I, pp. 125-28 *infra*).

country (which turns the "local" basis into a "national" basis), or even the whole world, since the depletion deduction is available to producers subject to the United States income tax regardless of where their mines are located.

Aside from the difficulties of determining the relevant area, there are other problems. For example:

(1) Is the "market or field price" to be computed "as of the date of sale" or as an average for some period? <sup>14</sup>

(2) In the case of fire clay, is such market price to be computed on the basis of an overall average of the unit prices at which all kinds of fire clay were sold, even though there are many varieties of fire clays which vary widely in utility and value? <sup>15</sup>

(3) Are the prices of fire clay and shale sold as by-products by coal strip miners relevant in determining the depletion deduction of producers of fire clay and shale from underground mines? <sup>16</sup>

<sup>14</sup> The regulation, note 13, p. 110 *supra*, contemplates the use of the price "as of the date of sale," thus requiring a day to day determination.

<sup>15</sup> Even on the basis of the statistics on which the Government relies, the average value per ton of fire clay sold by producers in 1951 varied from \$1.35 in the State of Washington to \$8.63 in New Jersey. U. S. BUREAU OF MINES, DEPT. OF INTERIOR, 1951 MINERALS YEARBOOK 294. This information would, in any event, be of no help to a taxpayer in filing his return, because of the delay in its publication. For example, the Minerals Yearbook for 1951 was not published until 1954.

<sup>16</sup> Use of such prices in the Brazil, Indiana, area to determine this taxpayer's depletion base would deny taxpayer any percentage depletion at all, because of the limitation of the deduction to 50% of net income "from the property."

If the Government says a market price is not to be used, it may turn to the "proportionate profits" method described in the regulations.<sup>17</sup> This method allocates gross income to the various processes on the basis of proportionate costs. The Government's brief does not assert that it should be used in this case. Determinative as far as this case is concerned, however, is the fact that in the District Court, both in its Pre-Trial Brief (pp. 6-7) and in its Post-Trial Brief (pp. 6, 18-19), the Government made it clear that it was not urging or relying on this method because it had been "abrogated" and had been "abandoned" by the Internal Revenue Service.<sup>18</sup>

**C. The Government's theories cannot be applied consistently with the legislative intent in other factual situations.**

Although the Court is expected to decide only the case before it, it seems appropriate to call the Court's attention to the confusion and illogical results which would be caused by the application of the Government's theories to other factual situations.

For example, a talc producer makes two entirely different products by entirely different processes: (1) pulverized talc, the product which the great majority of

<sup>17</sup> U. S. Treas. Reg. 111, § 29.23(m)-1(f) (Resp. App. 1, pp. 125-28 *infra*).

<sup>18</sup> The Treasury's Proposed Regulations, Section 1.613-3(b), defining "gross income from the property" under the Internal Revenue Code of 1954, also abandoned this method and substituted three alternatives. These Proposed Regulations were issued on November 3, 1956; Fed. Reg. Vol. 21, No. 215, p. 8439 at 8450, but have not yet been adopted. The proposed new methods are discussed and criticized in the House Hearings, 1959, pp. 267-69.



talc producers make and sell; and (2) sawed talc crayons which are much more expensive because suitable talc is rare.<sup>19</sup> If pulverized talc is the "basic mineral product,"<sup>20</sup> how is "gross income from the property" to be computed in the case of the more valuable talc used for crayons which are produced by different processes? If the only ordinary treatment processes are those applied to obtain the pulverized talc, so that there would be no "ordinary treatment processes" applied to obtain the crayons, then some "value" for raw talc must be used (although there is no market for it) and the taxpayer's deduction may well be smaller in the case of the more valuable talc.

In a similar situation involving a stone quarry producing both dimension (building) stone and crushed stone from different grades of stone, the Government argued that the market price per ton of crushed stone should be applied in computing the deduction for the dimension stone.<sup>21</sup> If this method (which does not recognize the greater value of the stone suitable for dimension stone) is to be used, then how is the "net income of the taxpayer . . . from the property" to be computed for purposes of the statutory limitation of the deduction to 50% of such net income? The processing of, and therefore the costs to produce, the two prod-

<sup>19</sup> See Record Appendix to Brief for Appellant, pp. 62, 115-16, 140, 184-87, *Townsend v. The Hitchcock Corp.*, 232 F.2d 444 (4th Cir. 1956).

<sup>20</sup> In 1954, Congress specifically listed the pulverization of talc as an "ordinary treatment process." INT. REV. CODE OF 1954, § 613(c) (4) (E) (Resp. App. II, p. 114).

<sup>21</sup> *Albin C. Halquist*, 33 T.C. 304 (1959) (Resp. App. II, p. 44).

ucts are entirely different. Application of the per ton cost of crushed stone to dimension stone involves pure speculation, especially for those producers of dimension stone who produce no crushed stone at all.

The Government invites this Court to overrule the *Merry Brothers* line of cases involving brick and tile clay. (Br. 18-19, 90-91) There is no market for such clay anywhere in the country to provide what the Government calls (Br. 18) "conclusive proof" of the point at which such clay is "fit for commercial or industrial use." Is the clay, then, "fit for commercial or industrial use" as it comes from the ground, as it enters the pugmill (the "cut-off point" first adopted by the Commissioner under his 1953 regulation),<sup>22</sup> or at some other point? If the first process after extraction is not included, there are no "ordinary treatment processes" as to brick and tile clay; if it is included, then there is no logical or reasonable basis for saying that "industrial use" begins with any one of the succeeding processes as distinguished from any other.<sup>23</sup>

Any explanation the Government may give of how the depletion deduction should be computed in these

<sup>22</sup> Rev. Rul. 54-109, 1954-1 CUM. BULL. 62 (Resp. App. II, pp. 161-62).

<sup>23</sup> The uncertainty is shown by *Cherokee Brick & Tile Co. v. United States*, 122 F. Supp. 59, 65 (M.D. Ga. 1954), *aff'd*, 218 F. 2d 424 (5th Cir. 1955):

"The defendant here contended that mining ceased after the fifth process [i.e., before final grinding, 122 F. Supp. at 61] but in argument admitted that it might be that it should include one or two more of the processes. . . . The difficulty of finding a definite 'cut off point' in this case clearly shows the difficulty which may frequently arise in attempting to apply such a definition as that contended for by the defendant."

various situations will of necessity involve arbitrary distinctions and theoretical computations which will produce results inconsistent with the legislative intent.

**D. The difficulties which the Government finds in the commercially marketable products rule are not persuasive.**

The Government's position against the commercially marketable products rule cannot be squared with the statutory language or the legislative history, and its criticisms of the rule have not persuaded Congress to change it. The Government, however, asks the Court to consider what it describes as the "extreme" results of the rule. The Government then proceeds to discuss what it considers the "implications" of the decision below. (Gov't Br. 22-25)

First, the Government claims that the lower court's interpretation of the statute will result in "sharp disparities and widespread discrimination" between the "integrated miner" and others. Certainly Congress meant to adopt the same rule, *i.e.*, the commercially marketable products rule, for computing percentage depletion for all miners of the same mineral (and indeed for all mine owners and operators), but this does not mean that Congress intended that all miners of the same mineral would be entitled to the same amount of depletion. A statute basing the depletion allowance on a percentage of "gross income from the property," limited to 50 percent of the taxpayer's net income from the property, obviously will result in different amounts of depletion allowances for miners of the same mineral. The Government's interpretation would limit the miner of a more valuable grade of a mineral to the same de-

pletion allowance as the operator of an inferior deposit, as the Government attempted to do in the *Iowa Limestone* case, pp. 64-66 *supra*. This would result in discrimination which clearly was not intended by Congress.

The Government has made no case that the "disparities" of which it complains are inconsistent with the Congressional intention. Its examples from the Record in this case are not convincing. As one example, the Government (Br. 22) describes a "non-integrated miner" in the same area as the taxpayer who was delivering fire clay and shale to a "local manufacturer" for \$1.40 a ton and says his depletion deduction would be 15 cents a ton. Actually, this "non-integrated miner" did not sell fire clay and shale, but was a contractor who extracted and hauled the clay and shale for the mine owner (the "local manufacturer" referred to by the Government) at a rate of \$1.40 a ton for his services. (See p. 69 n.22 *supra*) Since the contractor did not have any economic interest in the clay and shale deposit, *he was not entitled to any depletion allowance at all*. This is not discrimination. The Government also refers to the sale of fire clay and shale by coal strip miners in the Brazil, Indiana, area. (See pp. 5-6 *supra*) A Congressional purpose to encourage the discovery and exploitation of natural resources is inherent in percentage depletion, and it is not inconsistent with that purpose for the taxpayer to be entitled to a larger depletion allowance for fire clay and shale which it extracted from an underground mine and which made the best sewer pipe in Indiana than a

coal strip mine owner at Brazil who sold clay as a by-product. (See pp. 68-70 *supra*)

Second, the Government asserts that the holding below will encourage "vertical integration" and that the type of integration encouraged will be "upon a most inefficient basis," since the "view adopted below rewards the manufacturer who acquires an inefficient mine." There is nothing in this Record which warrants the inference that the taxpayer's mine was inefficient. (See pp. 68-69 *supra*)

The statute as written may well encourage the development of mines which otherwise would not be developed at all, but this is most consistent with the Congressional purpose in adopting percentage depletion. Whether it will result in the merger of existing economic entities is a question which could be answered reliably, if at all, only on the basis of an extensive economic study. Since Congress has not responded to the Treasury's pleas for amendatory legislation to avoid the result reached below (pp. 96-104 *supra*), it apparently is not alarmed about any such possibility. If the "vertical integration" which the Government somberly forecasts (Br. 89-90) should begin to occur, and if Congress should desire to do so, it can change the law.

Third, the Government claims that the "possibilities" for depletion allowances are "virtually limitless." It cites as illustrations pending cases which are not before this Court; it describes the taxpayers' claims in those cases but does not analyze the facts so that this Court may consider whether those claims have any foundation under the statute as construed by the courts.



The same may be said of the Government's estimates in its petition for certiorari (pp. 7-8 and App. C), referred to again in its brief (p. 24), of the "enormous" potential impact upon the revenue. The Government's estimate of the "annual potential tax loss" (Pet. for Cert., App. C, Table II) admittedly ignores the net income limitation. More important, the estimates assume the lack of a market for all minerals in the tables before they are processed into some "manufactured product," although the applicability of the commercially marketable products rule depends entirely on the factual question of marketability.

Finally, the Government states that the administrative problems are "grave," complaining that under the decision below the Commissioner "may not determine, for each of the various segments of the mining industry, the basic mineral product which establishes the cut-off point." (Br. 24) Congress did not specify such a "basic mineral product" for each "segment of the mining industry," and as we have shown, the statutory language and legislative history make it quite clear that Congress did not intend to give the Commissioner such broad administrative discretion. As we have also shown (pp. 109-15 *supra*), the administrative problems under the Government's interpretation of the statute would be quite difficult, and the Government has given no indication of how it would solve them. Furthermore, we submit that the Government exaggerates in saying that the difficulties of determining what products each mine operator can sell on a commercial basis are so great that "the Commissioner, in most instances,

would be obliged to presume that the finished products actually manufactured by an integrated producer are the only ones which he could profitably market." (Br. 24-25) This pessimistic prediction considerably overestimates the diversity of situations which will be encountered, and it considerably underestimates the expertness, resourcefulness, and determination to protect the revenue which are characteristic of the Revenue Service.

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In order to avoid the administrative problems as well as the other difficulties which the Government envisions in the commercially marketable products rule, the Government would leave to the Commissioner's discretion the determination of the "cut-off" points for various minerals. The Commissioner would then have a free hand to distinguish "mining" from "manufacturing," since the indefinite term "fit for commercial or industrial use" can provide no real standard or guide.<sup>24</sup> Congress specifically enacted the commercially marketable products rule because the Commissioner was making an arbitrary distinction between "mining" and "manufacturing." Congress has consistently refused to change that rule, although the Treasury has repeatedly

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<sup>24</sup> Even when the Treasury, in asking Congress in 1959 to abolish the commercially marketable products test, attempted to spell out in detail in its draft of legislation the processes which would be allowable in computing the depletion base, members of Congress feared that the Treasury's distinction between "mining" and "manufacturing" was too vague and granted too much power to the Commissioner (pp. 100-04 *supra*).

requested it to do so in order to restore the Commissioner's discretion.

In sum and substance, the Government now asks this Court to do what Congress has steadfastly refused to do, and this is an area which is peculiarly one for legislative judgment. *Cf. Helvering v. Griffiths*, 318 U.S. 371 (1943).

### CONCLUSION

The judgment of the Court of Appeals should be affirmed; in the alternative, the writ of certiorari should be dismissed.

Respectfully submitted,

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## APPENDIX I.

## Internal Revenue Code of 1939:

## Sec. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

\* \* \* \*

(m) *Depletion*.—In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner, with the approval of the Secretary. . . .

(n) *Basis for Depreciation and Depletion*.—The basis upon which depletion, exhaustion, wear and tear, and obsolescence are to be allowed in respect of any property shall be as provided in section 114.

[26 U.S.C., 1952 Ed., Sec. 23.]

## Sec. 114. BASIS FOR DEPRECIATION AND DEPLETION.

\* \* \* \*

(b) *Basis for Depletion*.—

\* \* \* \*

(4) [As amended by Sec. 145 of the Revenue Act of 1942, c. 619, 56 Stat. 798, and Sec. 319 (a) of the Revenue Act of 1951, c. 521, 65 Stat. 452.] *Percent-*

*age depletion for coal and metal mines and for certain other mines and natural mineral deposits.—*

(A) *In general.*—The allowance for depletion under section 23 (m) in the case of the following mines and other natural deposits shall be:

(i) in the case of sand, gravel, slate, stone (including pumice and scoria), brick and tile clay, shale, oyster shell, clam shell, granite, marble, sodium chloride, and, if from brine wells, calcium chloride, magnesium chloride, and bromine, 5 per centum,

(ii) in the case of coal, asbestos, brucite, dolomite, magnesite, perlite, wollastonite, calcium carbonates, and magnesium carbonates, 10 per centum,

(iii) in the case of metal mines, apatite, bauxite, fluorspar, flake graphite, vermiculite, beryl, garnet, feldspar, mica, talc (including pyrophyllite), lepidolite, spodumene, barite, ball clay, sagger clay, china clay, phosphate rock, rock asphalt, trona, bentonite, gilsonite, thenardite, borax, fuller's earth, tripoli, refractory and fire clay, quartzite, diatomaceous earth, metallurgical grade limestone, chemical grade limestone, and potash, 15 per centum, and

(iv) in the case of sulfur, 23 per centum of the gross income from the property during the taxable year, excluding from such gross income an amount equal to any rents or royalties paid or incurred by the taxpayer in respect of the



property. Such allowance shall not exceed 50 per centum of the net income of the taxpayer (computed without allowance for depletion) from the property, except that in no case shall the depletion allowance under section 23 (m) be less than it would be if computed without reference to this paragraph.

(B) [As added by Sec. 124 (c) of the Revenue Act of 1943, c. 63, 58 Stat. 26, and amended by Sec. 207 (a) of the Revenue Act of 1950, c. 994, 64 Stat. 906, and Sec. 304 (d) of the Excess-Profits Tax Act of 1950, c. 1199, 64 Stat. 1137.] *Definition of*

*gross income from property.*—As used in this paragraph the term “gross income from the property” means the gross income from mining. The term “mining” as used herein shall be considered to include not merely the extraction of the ores or minerals from the ground but also the ordinary treatment processes normally applied by mine owners or operators in order to obtain the commercially marketable mineral product or products, and so much of the transportation of ores or minerals (whether or not by common carrier) from the point of extraction from the ground to the plants or mills in which the ordinary treatment processes are applied thereto as is not in excess of 50 miles unless the Secretary finds that the physical and other requirements are such that the ore or mineral must be transported a greater distance to such plants or mills. The term “ordinary treatment processes”, as used herein, shall include the

following: (i) In the case of coal—cleaning, breaking, sizing, and loading for shipment; (ii) in the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment; (iii) in the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering to bring to shipping grade and form, and loading for shipment; and (iv) in the case of lead, zinc, copper, gold, silver, or fluor-spar ores, potash, and ores which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation (but not including as an ordinary treatment process electrolytic deposition, roasting, thermal or electric smelting, or refining), or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the ore, including the furnacing of quicksilver ores. The principles of this subparagraph shall also be applicable in determining gross income attributable to mining for the purposes of sections 450 and 453.

## Treasury Regulations 111: .

**Sec. 29.23 (m)-1. Depletion of Mines, Oil and Gas Wells, Other-Natural Deposits, and Timber . . .**

\* \* \* \* \*

[As amended by T.D. 5413, 1944 CUM. BULL. 124; T.D. 5458, 1945 CUM. BULL. 45; T.D. 5461, 1945 CUM. BULL. 284; T.D. 6004, 1953-1 CUM. BULL. 45; T.D. 6031, 1953-2 CUM. BULL. 120. **Note: The matter added to the Regulation on July 14, 1953, by T.D. 6031 is italicized. The words in brackets were deleted by T.D. 6031.**]

(f) The term "gross income from the property", as used in Sections 114(b)(3) and 114(b)(4)(A) and Sections 29.23 (m)-1 to 29.23 (m)-19, inclusive, means the following:

\* \* \* \* \*

If the taxpayer sells the crude mineral product of the property in the immediate vicinity of the mine, "gross income from the property" means the amount for which such product was sold, but, if the product is transported or processed (other than by the ordinary treatment processes described below) before the sale, "gross income from the property" means the representative market or field price (as of the date of sale) of a mineral product of like kind and grade as benefited by the ordinary treatment processes actually applied, before transportation of such product (other than transportation treated, for the taxable year, as mining). If there is no such representative market or field price

(as of the date of sale), then there shall be used in lieu thereof the representative market or field price of the first marketable product resulting from any process or processes (or, if the product in its crude mineral state is merely transported, the price for which sold) minus the costs and proportionate profits attributable to the transportation (other than transportation treated, for the taxable year, as mining) and the processes beyond the ordinary treatment processes. If the taxpayer establishes to the satisfaction of the Commissioner that another method of computation, other than the computation of profits proportionate to costs, clearly reflects the gross income from the property, then such gross income shall be computed by the use of such other method. For a description of transportation which is treated, for taxable years beginning after December 31, 1949, as mining, see the preceding paragraph and Section 114(b)(4)(B), as amended.

The term "ordinary treatment processes", as used herein, shall include the following:

- (1) In the case of coal—cleaning, breaking, sizing, and loading for shipment;
- (2) In the case of sulphur—pumping to vats, cooling, breaking, and loading for shipment;
- (3) In the case of iron ore, bauxite, ball and sagger clay, rock asphalt, and minerals which are customarily sold in the form of a crude mineral product—sorting, concentrating, and sintering (*agglomerating by in-*

*ipient fusion*) to bring to shipping grade and form, and loading for shipment;

(4) In the case of lead, zinc, copper, gold, silver, or fluorspar ores, potash and *minerals* [ores] which are not customarily sold in the form of the crude mineral product—crushing, grinding, and beneficiation by concentration (gravity, flotation, amalgamation, electrostatic, or magnetic), cyanidation, leaching, crystallization, precipitation, or by substantially equivalent processes or combination of processes used in the separation or extraction of the product or products from the *mineral* [ore]. The furnacing of quicksilver ores is included in the term “ordinary treatment processes”. The following processes are not included in the term “ordinary treatment processes”: electrolytic deposition, roasting, thermal or electric smelting, refining, or substantially equivalent processes.

*In addition, the processes listed below are not included in the term “ordinary treatment processes” unless such processes are (i) otherwise provided for in (1), (2), (3), or (4) above; (ii) necessary or incidental to the processes provided for in (1), (2), (3), or (4) above; or (iii) necessary to bring the ores or minerals into condition or form suitable for shipment (for example, the agglomeratton of concentrates):*

(A) *treatment effecting a chemical change;*

(B) *blending with other material;*

(C) *thermal action;*

(D) *fine pulverization, pressing into shape, or molding.*



*For the purposes of (3) and (4) above, the terms "concentration" or "concentrating" mean the process of eliminating waste or of separating two or more minerals or ores.*

\* \* \* \* \*

(128-9)